MASTER
NEGATIVE
NO. 94-82065-7

COPYRIGHT STATEMENT

The copyright law of the United States (Title 17, United States Code) governs the making of photocopies or other reproductions of copyrighted materials including foreign works under certain conditions. In addition, the United States extends protection to foreign works by means of various international conventions, bilateral agreements, and proclamations.

Under certain conditions specified in the law, libraries and archives are authorized to furnish a photocopy or other reproduction. One of these specified conditions is that the photocopy or reproduction is not to be "used for any purpose other than private study, scholarship, or research." If a user makes a request for, or later uses, a photocopy or reproduction for purposes in excess of "fair use," that user may be liable for copyright infringement.

The Columbia University Libraries reserve the right to refuse to accept a copying order if, in its judgement, fulfillment of the order would involve violation of the copyright law.

Author:
Finney, Harry Anson

Title:
Consolidated statements for holding company...

Place:
New York

Date:
1923

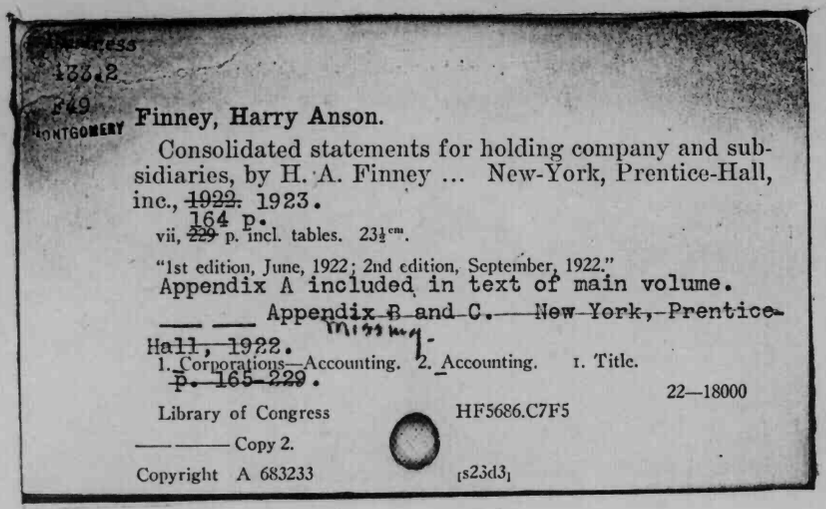
94-82065-7

MASTER NEGATIVE #

COLUMBIA UNIVERSITY LIBRARIES
PRESERVATION DIVISION

BIBLIOGRAPHIC MICROFORM TARGET

ORIGINAL MATERIAL AS FILMED - EXISTING BIBLIOGRAPHIC RECORD



[illegible]ress
138.2
F49
MONTGOMERY

Finney, Harry Anson.

Consolidated statements for holding company and subsidiaries, by H. A. Finney ... New-York, Prentice-Hall, inc., ~~1922.~~ 1923.
~~164~~ p.
vii, ~~229~~ p. incl. tables. 23½ cm.

"1st edition, June, 1922; 2nd edition, September, 1922."
Appendix A included in text of main volume.
~~__ __ Appendix B and C. New York, Prentice-Hall, 1922.~~
1. Corporations—Accounting. 2. Accounting. 1. Title.
~~p. 165-229.~~

22—18000

Library of Congress HF5686.C7F5

~~_____~~ Copy 2.

Copyright A 683233 [s23d3]

RESTRICTIONS ON USE:

TECHNICAL MICROFORM DATA

FILM SIZE: 35mm REDUCTION RATIO: 12x IMAGE PLACEMENT: IA (IIA) IB IIB

DATE FILMED: 5/3/94 INITIALS: W.W

TRACKING # : MSH 00722

FILMED BY PRESERVATION RESOURCES, BETHLEHEM, PA.

2.0 mm ABCDEFGHIJKLMNOPQRSTUVWXYZ
abcdefghijklmnopqrstuvwxyz1234567890

1.5 mm ABCDEFGHIJKLMNOPQRSTUVWXYZ
abcdefghijklmnopqrstuvwxyz1234567890

PM-MGP 13″x18″
METRIC GENERAL PURPOSE TARGET
PHOTOGRAPHIC

150 mm

100 mm

1.0 mm

1.5 mm

2.0 mm

2.5 mm

A5

A4

PRECISION℠ RESOLUTION TARGETS

Century

A&P

1303 Geneva Avenue
St. Paul, MN 55119

ABCDEFGHIJKLMNOPQRSTUVWXYZ
abcdefghijklmnopqrstuvwxyz
1234567890

4.5 mm

ABCDEFGHIJKLMNOPQRSTUVWXYZ
abcdefghijklmnopqrstuvwxyz1234567890

3.5 mm

433.2 F49
Columbia University
in the City of New York
LIBRARY

School of Business

School of Business Library
Columbia University
APR 8 1942

CONSOLIDATED STATEMENTS

FOR HOLDING COMPANY AND SUBSIDIARIES

BY

H. A. FINNEY, PH. B., C. P. A.

PROFESSOR OF ACCOUNTING, NORTHWESTERN UNIVERSITY, CHICAGO

NEW YORK

PRENTICE-HALL, INC.

1924

D
433.2
F49
(replace copy)
uncat

650-36657

COPYRIGHT, 1922, BY
PRENTICE-HALL, INC.

1st Printing.....June, 1922
2nd Printing....September, 1922
3rd Printing.....March, 1923
4th Printing.....August, 1924

PRINTED IN THE UNITED STATES OF AMERICA

TO
MY WIFE AND MY MOTHER

PREFACE

This book is intended to embrace the principles and procedure involved in the preparation of the consolidated statement of cost of goods sold, the consolidated profit and loss statement, the consolidated surplus statement and the consolidated balance sheet.

Students of accounting who are preparing for the examinations of the various C. P. A. boards or the American Institute of Accountants must be familiar with the subject of consolidated statements for holding companies and their subsidiaries, for the examinations frequently contain more or less complicated problems requiring the preparation of such statements. The income tax law, which requires consolidated returns supported by consolidated income statements and balance sheets, makes a knowledge of the method of preparing these statements imperative for the corporation auditor, the public accountant and the tax counsellor.

It is surprising that the literature which deals with consolidated statements is so meager when one considers that so many accountants and students of accounting are interested in the subject and that the statements themselves may be involved by an almost infinite variety of complications. These complexities arise from the fact that the holding company may or may not account properly for the investments in subsidiary stock; that minority interests may exist; that subsidiary earnings since acquisition may exceed dividends received during the same period, or vice versa; that the holding company may take up as profit the earnings of the subsidiary or the dividends received; that the stock may have been acquired by purchase from former stockholders, by subscription or as a stock dividend; that book value at acquisition may have exceeded cost, or vice versa; that the stockholdings may have been acquired by a single purchase or by several purchases; that the holdings may be in common or preferred stock or both; that inter-company profits may remain unrealized in inventories and in fixed assets; etc., etc.

The book contains a discussion of underlying principles, illustrations showing the procedure of preparing consolidated working papers and statements, and supplementary exercises and problems to be solved by the reader.

On several phases of consolidated statements there is some conflict of opinion as to the proper procedure and considerable variation in practice. This is particularly true in the matters of minority interest in a subsidiary with a deficit, negative goodwill, and reserves for unrealized profit when there are minority interests. Where practice has not been standardized the fact is commented upon, the different methods of procedure are discussed, and the method which seems to the author to be correct in principle is indicated.

It scarcely seems necessary to remind the reader that accounting principles and income tax regulations do not always coincide. Taxable net income and invested capital do not always agree with the figures shown in the revenue statement and the balance sheet, yet these statements are the basis of a corporation's tax return, and the consolidated profit and loss statement and balance sheet are the basis of a consolidated return. This book is not an interpretation of the regulations pertaining to consolidated returns, but is an explanation of the accounting principles underlying the consolidated statements which must be submitted in support of the return.

The author wishes to acknowledge his obligation to his friend Roy Hall, C.P.A., who read the manuscript and offered helpful criticisms and suggestions.

H. A. FINNEY

Chicago, Illinois
May 15, 1922

CONTENTS

CHAPTER		PAGE
I.	CONSOLIDATIONS, MERGERS, HOLDING COMPANIES	1
II.	THE BALANCE SHEET OF A HOLDING COMPANY	9
III.	SUBSIDIARY SURPLUS OR DEFICIT AT ACQUISITION	16
IV.	MINORITY INTEREST	20
V.	GOODWILL	25
VI.	DEDUCTION FROM GOODWILL	34
VII.	SUBSIDIARY'S PROFITS, LOSSES AND DIVIDENDS ON THE HOLDING COMPANY'S BOOKS	42
VIII.	CONSOLIDATED BALANCE SHEET AFTER DATE OF ACQUISITION; SUBSIDIARY PROFITS AND LOSSES TAKEN UP	47
IX.	CONSOLIDATED BALANCE SHEET AFTER DATE OF ACQUISITION; INVESTMENT ACCOUNT CARRIED AT COST	54
	REVIEW EXERCISES	62
X.	INTER-COMPANY RECEIVABLES AND PAYABLES	65
XI.	MISCELLANEOUS TOPICS:	
	Book Value at Acquisition in Excess of Cost	74
	Minority Interest in a Subsidiary with a Deficit	75
	Stock Acquired by Subscription from Subsidiary	78
	Subscription Rights	79
	No Par Value Stock	81
	Holdings of Both Common and Preferred Stock	81
	Stock Dividends	85
	Arbitrary Entries in Investment Account	87
XII.	MAJOR HOLDING COMPANY CONTROL THROUGH A MINOR HOLDING COMPANY	89
XIII.	UNREALIZED INTER-COMPANY PROFITS	103
XIV.	CONSOLIDATED PROFIT AND LOSS AND SURPLUS STATEMENTS; SEPARATE WORKING PAPERS	110
XV.	CONSOLIDATED PROFIT AND LOSS STATEMENT, SURPLUS STATEMENT AND BALANCE SHEET; COMBINED WORKING PAPERS	128
	PROBLEMS	151

CHAPTER I

CONSOLIDATIONS, MERGERS, HOLDING COMPANIES

Methods of effecting combinations.—When it is desired to combine two or more corporations into a single company or into a co-ordinated organization with a centralized control, the result may be accomplished by several means, the most common of which are a consolidation, a merger, and a holding company.

As a simple illustration of these three methods of effecting combinations, it will be assumed that the two companies whose balance sheets appear below are to be combined.

BALANCE SHEET—COMPANY A

Machinery	$25,000	Accounts Payable	$10,000
Merchandise Inventory	15,000	Capital Stock	35,000
Cash	5,000		
	$45,000		$45,000

BALANCE SHEET—COMPANY B

Machinery	$35,000	Accounts Payable	$15,000
Merchandise Inventory	25,000	Capital Stock	50,000
Cash	5,000		
	$65,000		$65,000

Consolidation.—A consolidation is effected by organizing a new corporation which buys the assets and assumes the liabilities of the old companies. The new company may sell its stock for cash and pay the old companies in cash for their net assets, or it may issue its stock to the old companies in payment for their net assets. In either case the old companies go out of existence, distributing among their stockholders the cash or stock received from the new company.

To illustrate, it will be assumed that Company C is organized with a capital stock of $85,000; and contracts are entered into with Company A and Company B whereby it is agreed that Company C shall take over the assets of the two companies at their book value, assume their liabilities, and pay for the net assets in stock of Company C.

Entries of the consolidating company.—Company C will make the following entries to record the consolidation:

Subscriptions		$85,000	
Capital Stock			$85,000
To record the subscriptions to our entire authorized stock issue, as follows:			
Company A	$35,000		
Company B	50,000		
Total	$85,000		
Machinery		$25,000	
Merchandise Inventory		15,000	
Cash		5 000	
Accounts Payable			$10,000
Company A, Vendor			35,000
To record the purchase of the assets of Company A and the assumption of their liabilities, in accordance with the contract dated ———. Payment to be made in the stock of this company.			
Company A, Vendor		35,000	
Subscriptions			35,000
To record the offset of our liability to Company A for their net assets against their liability to us on account of subscriptions to our stock.			
Machinery		$35,000	
Merchandise Inventory		25,000	
Cash		5,000	
Accounts Payable			15,000
Company B, Vendor			50,000
To record the purchase of the assets of Company B and the assumption of their liabilities, in accordance with the contract dated ———. Payment to be made in the stock of this company.			
Company B, Vendor		$50,000	
Subscriptions			$50,000
To record the offset of our liability to Company B for their net assets against their liability to us on account of subscriptions to our stock.			

Balance sheet of the consolidation.—After the consolidation has been effected, the balance sheet of the new company will show all of the assets and liabilities formerly owned by the old companies, and now owned by the new or consolidated company.

BALANCE SHEET—COMPANY C

Machinery	$60,000	Accounts Payable	$25,000
Merchandise Inventory	40,000	Capital Stock	85,000
Cash	10,000		
	$110,000		$110,000

Entries of the absorbed companies.—The entries of Company A and Company B will be similar to each other and will show the sale of their assets to Company C, the assumption of their liabilities by Company C, the receipt of stock in payment for their net assets, and the distribution of this stock among their stockholders. These entries will be illustrated by showing those which will appear on the books of Company A.

Company C, Vendee	$35,000	
Accounts Payable	10,000	
Machinery		$25,000
Merchandise Inventory		15,000
Cash		5,000
To record the sale of our assets to Company C and the assumption by them of our liabilities; payment for net assets to be made in stock of Company C, in accordance with the contract of sale dated ———. See Minutes, page —.		
Stock of Company C	$35 000	
Company C, Vendee		$35,000
To record the receipt of stock of Company C in payment for net assets transferred to them.		
Captal Stock	$35,000	
Stock of Company C		$35,000
To record the distribution of the stock of Company C among our stockholders in final liquidation of this company.		

Thus it will be seen that Company A and Company B go out of existence. They have no assets nor liabilities, and all of the assets and liabilities of the consolidation are shown on the balance sheet of Company C.

Merger.—If a merger is decided upon, a new corporation will not be organized. One of the old companies will purchase

the assets and assume the liabilities of the other company, paying for the net assets either in cash or in stock. As the company which has been bought out will go out of existence, the merger as well as the consolidation results in a complete combination of the two old companies into a single company.

To illustrate, it will be assumed that Company A contracts with Company B to purchase its assets at book value, assume its liabilities, and pay for the net assets in stock of Company A. In order to provide the necessary stock for this purpose, Company A increases its authorized capitalization from $35,000 to $85,000.

Entries of the purchasing company.—Company A will make the following entries to record the merger:

Subscriptions	$50,000	
Capital Stock		$50,000
To record an addition of $50,000 to our authorized stock, all of which has been subscribed for by Company B, to be paid for by a transfer of their net assets.		
Machinery	$35,000	
Merchandise Inventory	25,000	
Cash	5,000	
Accounts Payable		$15,000
Company B, Vendor		50,000
To record the purchase of the assets of Company B and the assumption of their liabilities, in accordance with the contract dated ———. Payment for the net assets to be made in the stock of this company.		
Company B, Vendor	$50,000	
Subscriptions		$50,000
To record the offset of our liability to Company B for their net assets against their liability to us on account of subscriptions to our stock.		

Balance sheet of the merger.—After the merger has been effected, the balance sheet of Company A will show all of the assets and liabilities formerly shown by the balance sheets of the two companies.

BALANCE SHEET—COMPANY A

Machinery	$60,000	Accounts Payable	$25,000
Merchandise Inventory	40,000	Capital Stock	85,000
Cash	10,000		
	$110,000		$110,000

Entries of the absorbed company.—Company B will make entries to record the transfer of its assets and liabilities to Company A, the receipt of the stock in settlement, and the distribution of this stock among its own stockholders.

Company A, Vendee	$50,000	
Accounts Payable	15,000	
Machinery		$35,000
Merchandise Inventory		25,000
Cash		5,000
To record the sale of our assets to Company A and the assumption by Company A of our liabilities; payment for net assets to be made in stock of Company A, in accordance with the contract of sale dated ———. See Minutes, page —.		
Stock of Company A	$50,000	
Company A, Vendee		$50,000
To record the receipt of stock of Company A in payment for the net assets transferred to them.		
Capital Stock	$50,000	
Stock of Company A		$50,000
To record the distribution of the stock of Company A among our stockholders in final liquidation of this company.		

Thus it will be seen that Company B goes out of existence; it has no assets nor liabilities, and all of the assets and liabilities of the merged companies are shown in the balance sheet of Company A.

Holding company.—If the holding company procedure is adopted, one of the old companies may act as the holding company, or a new corporation may be organized to act in that capacity. The holding company does not deal directly with the other companies, and does not buy their assets nor assume their liabilities. It deals with the stockholders of the old companies, buying all of, or a controlling interest in, their stock. The company acquiring the stock is called a holding company or parent company, and the companies whose stock is acquired by the holding company are called subsidiaries.

The holding company may pay for the subsidiary stock in cash, and if this is done the former stockholders of the subsidiaries do not become stockholders of the holding company. On the other hand, the holding company may issue its own stock in payment for the acquired stock, and if this is done the former stockholders of the subsidiaries become stockholders of the holding company.

Outline of illustrations.—Three illustrations of the holding company procedure will be given in this chapter, which may be divided into two groups as follows:

Group I. New corporation organized to act as holding company.
- First illustration: Stockholders of old companies receive stock in payment.
- Second illustration: Stockholders of old companies receive cash in payment.

Group II. One of the old companies acts as holding company.
- Third illustration: Stockholders of subsidiary receive stock in payment.

First illustration.—It will be assumed in this illustration that a new corporation called Company C is organized to act as a holding company. Its charter authorizes it to issue stock totalling $85,000. All of the stockholders of Company A and Company B agree to sell their holdings in these companies to Company C, taking in payment therefor an equal number of shares of the stock of Company C.

The entries on the books of Company C, the holding company, are:

Subscriptions	$85,000	
Capital Stock		$85,000
To record subscriptions to our stock as follows:		
Stockholders of Company A	$35,000	
Stockholders of Company B	50,000	
Total	$85,000	
Investment in Stock of Company A	$35,000	
Investment in Stock of Company B	50,000	
Subscriptions		$85,000
To record the payment of subscriptions by transfer to us of stock of Company A and Company B.		

The balance sheet of the holding company will appear as follows:

BALANCE SHEET—COMPANY C

Investment in Stock of Co. A	$35,000	Capital Stock	$85,000
Investment in Stock of Co. B	50,000		
	$85,000		$85,000

The only entries on the books of Companies A and B will be made in their stock ledgers, recording the transfer of stock from the sundry stockholders to Company C. These companies are not parties to the transaction, they retain the same assets and liabilities as before, and their balance sheets are not affected by the change in the ownership of their stock.

Second illustration.—It will be assumed, in this illustration, that the new Company C sells its stock for cash to various individuals not formerly stockholders of either Company A or Company B, and with the proceeds of the stock issue it buys at par all of the stock of the two original companies.

The entries on Company C's books are as follows:

Subscriptions	$85,000	
Capital Stock		$85,000
To record the subscriptions to our authorized issue		
Cash	$85,000	
Subscriptions		$85,000
To record the collection of subscriptions		
Investment in Stock of Company A	$35,000	
Investment in Stock of Company B	50,000	
Cash		$85,000
To record the purchase of all of the outstanding stock of Companies A and B at par value		

The balance sheet of the holding company will be exactly like the one shown in the first illustration, and the balance sheets of the subsidiary companies will be in no way affected by the transaction, since they still retain their assets and liabilities.

Third illustration.—It will be assumed in this illustration that Company A is to act as the holding company. It increases its authorized stock issue from $35,000 to $85,000; the additional stock is subscribed for by the stockholders of Company B, who pay their subscriptions by turning over their holdings of the stock of Company B. The entries on Company A's books are:

Subscriptions	$50,000	
Capital Stock		$50,000
To record the subscriptions to our additional authorized capital stock		
Investment in Stock of Company B	$50,000	
Subscriptions		$50,000
To record the payment of subscriptions in stock of Company B		

The balance sheet of the holding company after recording these transactions, will be:

COMPANY A—BALANCE SHEET

Investment in Stock of Co. B	$50,000	Accounts Payable	$10,000
Machinery	25,000	Capital Stock	85,000
Merchandise Inventory	15,000		
Cash	5,000		
	$95,000		$95,000

The balance sheet of Company B will not be affected by the transaction.

CHAPTER II

THE BALANCE SHEET OF A HOLDING COMPANY

Balance sheet after consolidation.—In the illustration on page 3 it was shown that if a combination is effected by means of a consolidation, one company will exist where several existed before, and the balance sheet of the new or consolidated company will show all of the assets and liabilities of the combined companies. The balance sheet of the consolidation shown on page 3 was:

BALANCE SHEET—COMPANY C

Machinery	$60,000	Accounts Payable	$25,000
Merchandise Inventory	40,000	Capital Stock	85,000
Cash	10,000		
	$110,000		$110,000

Company A and Company B went out of business and have no balance sheets.

Balance sheet after merger.—In the illustration on page 4 it was shown that if the combination was effected by means of a merger, one of the old companies would continue in existence and its balance sheet would show all of the assets and liabilities of the combined companies. The balance sheet after the merger, as shown on page 4, was exactly like the one of the consolidation, except that the assets and liabilities had passed to Company A instead of to Company C.

BALANCE SHEET—COMPANY A

Machinery	$60,000	Accounts Payable	$25,000
Merchandise Inventory	40,000	Capital Stock	85,000
Cash	10,000		
	$110,000		$110,000

Balance sheets of parent and subsidiaries.—In the first holding company illustration, on page 6, the balance sheets

of the several companies after effecting the combination, were:

BALANCE SHEET—COMPANY C

Investment in Stock of Co. A.	$35,000	Capital Stock.....	$85,000
Investment in Stock of Co. B.	50,000		
	$85,000		$85,000

BALANCE SHEET—COMPANY A

Machinery.....	$25,000	Accounts Payable.....	$10,000
Merchandise Inventory.....	15,000	Capital Stock.....	35,000
Cash.....	5,000		
	$45,000		$45,000

BALANCE SHEET—COMPANY B

Machinery.....	$35,000	Accounts Payable.....	$15,000
Merchandise Inventory.....	25,000	Capital Stock.....	50,000
Cash.....	5,000		
	$65,000		$65,000

The balance sheets in the second holding company illustration, on page 7, would be exactly like those in the first illustration.

In the third illustration, on page 7, it was assumed that Company A acted as the holding company, and the resulting balance sheets were:

BALANCE SHEET—COMPANY A

Investment in Stock of Co. B.	$50,000	Accounts Payable.....	$10,000
Machinery.....	25,000	Capital Stock.....	85,000
Merchandise Inventory.....	15,000		
Cash.....	5,000		
	$95,000		$95,000

BALANCE SHEET—COMPANY B

Machinery.....	$35,000	Accounts Payable.....	$15,000
Merchandise Inventory.....	25,000	Capital Stock.....	50,000
Cash.....	5,000		
	$65,000		$65,000

Object of the consolidated balance sheet.—When a combination is effected by means of a consolidation or a merger, a single balance sheet contains all of the assets and liabilities of the combined companies. But when the combination is effected by means of a holding company, each corporation maintains its separate legal entity and prepares its own balance sheet. These separate balance sheets are not a satisfactory means of displaying the financial condition of the several related companies for two reasons.

In the first place, if we view the several companies as separate corporations, the balance sheet of each company should clearly present the facts of its financial condition. The balance sheets of the subsidiary companies do so, since they show the assets and liabilities of these companies. The balance sheet of the holding company, however, fails to do so. The reason for this failure can be seen by referring to the balance sheet of Company C on page 10. This balance sheet contains two investment accounts, but there is nothing in the balance sheet to indicate exactly what these investments in stock represent. They represent the assets and liabilities of the subsidiary companies, and the balance sheet of the holding company would be a much clearer presentation of its financial condition if these investment accounts were dropped out of the balance sheet and replaced by the assets and liabilities of the subsidiaries. For while it is true from a legal standpoint that the holding company owns merely the stock, it is also true from a business standpoint that the holding company virtually owns and actually controls the subsidiary's net assets which the stock represents.

In the second place, if we look past the legal fiction of separate corporate entities and view the related companies as a single organization, we find that no single balance sheet shows the total assets and liabilities of the organization, and the total stock of the organization in the hands of the public.

The consolidated balance sheet is a device for avoiding these two disadvantages of separate balance sheets. The assets and liabilities of the several companies are all combined, with the exception of those accounts which represent merely intercompany relations. The investment accounts are not included among the assets on the consolidated balance sheet because these accounts do not represent assets in and of them-

selves but merely represent the holding company's right to the subsidiary's net assets. The capital stock accounts on the subsidiary's books represent the same inter-company relation if the stock is all owned by the holding company; and when this is the case no portion of the subsidiaries' capital stock is included in the consolidated balance sheet.

The consolidated balance sheet thus has its advantages whether we view the affiliated companies as separate entities or as a single organization. If we view them as separate corporations, the consolidated balance sheet is a more adequate presentation of the holding company's financial condition than is a balance sheet showing the investment accounts, for the consolidated balance sheet shows the total assets under the control of the holding company, the total liabilities to be paid out of these assets, and the capital of the holding company.

On the other hand, if we view the several companies as a single organization, the consolidated balance sheet shows the financial condition of this organization in relation to the outside world, for it combines all of the assets and liabilities of the related companies, it shows the total stock outstanding in the hands of the public, and it does not show mere inter-company relations as assets or liabilities of the organization.

Consolidated working papers.—From the discussion in the preceding section, it will be apparent that in preparing a consolidated balance sheet it is necessary to combine all similar assets and liabilities and eliminate all accounts showing mere inter-company relations. This work is facilitated by drawing up consolidated balance sheet working papers. These working papers contain columns for the several balance sheets to be consolidated, columns for accounts to be eliminated, and columns to contain the figures which are to appear in the consolidated balance sheet.

Outline of illustrations.—Two illustrations will be given in this chapter to show the method of preparing consolidated balance sheet working papers.

First illustration: Holding company is not an operating company, and has no assets other than its investments in subsidiaries.

Second illustration: Holding company is an operating company, and has assets other than its investment in a subsidiary.

First illustration.—This illustration is based on the balance sheets at the top of page 10 which show the financial condition of the related companies when a new corporation was organized to act as the holding company.

COMPANY C AND SUBSIDIARIES A AND B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

(Date)

Assets	*Co. C*	*Co. A*	*Co. B*	*Inter-Co. Eliminations*	*Consolidated B. S.*
Investment in Stock of Co. A	$35,000			$35,000	
Investment in Stock of Co. B	50,000			50,000	
Machinery		$25,000	$35,000		$60,000
Merchandise Inventory		15,000	25,000		40,000
Cash		5,000	5,000		10,000
	$85,000	$45,000	$65,000	$85,000	$110,000
Liabilities					
Accounts Payable		$10,000	$15,000		$25,000
Capital Stock:					
Co. C	$85,000				85,000
Co. A		35,000		35,000	
Co. B			50,000	50,000	
	$85,000	$45,000	$65,000	$85,000	$110,000

The following is the consolidated balance sheet prepared from these working papers.

COMPANY C AND SUBSIDIARIES A AND B

CONSOLIDATED BALANCE SHEET

(Date)

Machinery	$60,000	Accounts Payable	$25,000
Merchandise Inventory	40,000	Capital Stock	85,000
Cash	10,000		
	$110,000		$110,000

Second illustration.—This illustration is based on the balance sheets at the bottom of page 10, which show the financial condition of the related companies when one of the old companies acts as the holding company.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

(Date)

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Company B	$50,000		$50,000	
Machinery	25,000	$35,000		$60,000
Merchandise Inventory	15,000	25,000		40,000
Cash	5,000	5,000		10,000
	$95,000	$65,000	$50,000	$110,000
Liabilities				
Accounts Payable	$10,000	$15,000		$25,000
Capital Stock:				
Co. A	85,000			85,000
Co. B		50,000	$50,000	
	$95,000	$65,000	$50,000	$110,000

The consolidated balance sheet prepared from these working papers is as follows:

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Machinery	$60,000	Accounts Payable	$25,000
Merchandise Inventory	40,000	Capital Stock	85,000
Cash	10,000		
	$110,000		$110,000

Inter-company eliminations.—Reasons have already been given for the elimination of certain items in preparing the consolidated balance sheet, but these eliminations are so important that it may be well to re-state these reasons even though the re-statement be merely a reiteration.

It is to be borne in mind that the consolidated balance sheet is not the balance sheet of any one company, but is the balance sheet of a group of very closely affiliated companies showing the financial condition of the group of companies as if they were a single organization. The essential facts to be shown are: the total assets of the organization without omission or duplication, the total liabilities to the world outside the organization, and the total capital in the hands of the public.

When the group of companies is thus dealt with as a single company or organization, any inter-company relations become

virtually inter-departmental relations and have no place in a statement which is intended to show merely the relations of the organization to outsiders.

The investment accounts carried as assets on the holding company's books are therefore eliminated. These accounts merely represent the interest of the holding company in the subsidiary. They do not represent, in and of themselves, an asset which could be used to pay the liabilities of the organization. To include the assets of the subsidiary in the consolidated balance sheet and also the investment account would be a duplication and would result in an overstatement of the assets of the organization.

When all of the capital stock of the subsidiary is owned by the holding company, the capital stock account on the subsidiary's books does not represent a capital liability to the outside world. The only outstanding stock is that issued by the holding company. Therefore the subsidiary capital stock is dropped out in the Elimination column.

Chapter III

SUBSIDIARY SURPLUS OR DEFICIT AT ACQUISITION

Conditions common to preceding illustrations.—All of the holding company illustrations in the preceding chapters were made as simple as possible; in each of them the following conditions prevailed:

1. The consolidated balance sheet was prepared immediately after the holding company acquired its holdings in the subsidiary stock.
2. The holding company acquired all of the subsidiary stock.
3. The price paid was the exact book value of the acquired stock as shown by the subsidiary's books.
4. The subsidiary had no surplus or deficit at the date of acquisition; therefore the book value of its stock was represented by its capital stock account only.

All of these conditions may be changed, and each change will affect the procedure in preparing the consolidated balance sheet.

Outline of illustrations.—In the illustrations in this chapter, condition (1) will remain unchanged; the consolidated balance sheet will be prepared at the date of acquisition. Condition (2) will also remain unchanged; the holding company will own all of the subsidiary stock. Condition (3) will also remain unchanged; the purchase price will be exactly book value at the date of acquisition as shown by the subsidiary's books.

Condition (4) will be changed as follows: First illustration: the book value at the date of acquisition will be the sum of the capital stock and surplus accounts of the subsidiary; Second illustration: the book value at the date of acquisition will be the capital stock of the subsidiary minus its deficit account.

Subsidiary surplus at acquisition.—The reader is now familiar with the principle that accounts which merely represent inter-company relations are eliminated in the consolidated

working papers. In each preceding illustration the investment account in the holding company's balance sheet was eliminated because it represented the holding company's claim to the subsidiary's net assets; and the subsidiary's capital stock account was eliminated because it represented a capital liability of the subsidiary to the holding company.

If the subsidiary has a surplus at the date of acquisition, this account must be added to the capital stock account to determine the total capital; and if all of the stock is owned by the parent company, the surplus, as well as the capital stock, represents a capital liability to the holding company, and is subject to the principle which requires the elimination of inter-company accounts.

First illustration.—Company A has just purchased all of the stock of Company B, paying book value therefor. This book value is represented by the sum of the capital stock and surplus accounts on the books of Company B. The balance sheets of the two companies immediately following the stock purchase are as follows:

BALANCE SHEET—COMPANY A

Investment in Stock of Co. B.	$65,000	Accounts Payable	$10,000
Cash	20,000	Capital Stock	75,000
	$85,000		$85,000

BALANCE SHEET—COMPANY B

Cash	$70,000	Accounts Payable	$5,000
		Capital Stock	50,000
		Surplus	15,000
	$70,000		$70,000

The investment account of $65,000 represents the holding company's right to the net assets of the subsidiary; and the capital stock and surplus accounts on the subsidiary's books represent the offsetting capital liability of the subsidiary to the holding company. All are eliminated as showing mere inter-company relations.

The reason for the elimination of the subsidiary surplus can be further explained by reminding the reader that the consolidated balance sheet is virtually a balance sheet of the holding company, in which the investment account is dropped

out and replaced by the subsidiary assets and liabilities which it represents. It would clearly be wrong to carry out any of the subsidiary surplus to the consolidated balance sheet and thus imply that it was holding company surplus. The subsidiary surplus was built up from earnings prior to the date when the holding company acquired the stock.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Company B	$65,000		$65,000	
Cash	20,000	$70,000		$90,000
	$85,000	$70,000	$65,000	$90,000
Liabilities				
Accounts Payable	$10,000	$5,000		$15,000
Capital Stock:				
Co. A	75,000			75,000
Co. B		50,000	$50,000	
Surplus:				
Co. B		15,000	15,000	
	$85,000	$70,000	$65,000	$90,000

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$90,000	Accounts Payable	$15,000
		Capital Stock	75,000
	$90,000		$90,000

Subsidiary deficit at acquisition.—If the subsidiary has a deficit at the date of acquisition, this account must be deducted from the subsidiary's capital stock to determine its net capital. If the holding company acquires all of the subsidiary's stock, both the deficit and the capital stock must be considered in determining the capital liability of the subsidiary to the holding company, and both accounts are subject to the principle which requires the elimination of inter-company accounts.

Second illustration.—Company A has just purchased all of the stock of Company B, paying book value therefor. This book value is shown by the capital stock and deficit accounts on the subsidiary's books. The balance sheets of the two

companies need not be set out separately as all of the figures are shown in the first two columns of the working papers.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B	$45,000		$45,000	
Cash	35,000	$55,000		$90,000
Deficit—Co. B		15,000	15,000	
	$80,000	$70,000	$60,000	$90,000
Liabilities				
Accounts Payable	$20,000	$10,000		$30,000
Capital Stock:				
Co. A	50,000			50,000
Co. B		60,000	60,000	
Surplus—Co. A	10,000			10,000
	$80,000	$70,000	$60,000	$90,000

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$90,000	Accounts Payable	$30,000
		Capital Stock	50,000
		Surplus	10,000
	$90,000		$90,000

CHAPTER IV

MINORITY INTEREST

Minority interest an outside liability.—When the holding company acquires less than 100 per cent of the stock of the subsidiary, it shares the ownership of the subsidiary with outsiders whose stock it fails to purchase. These outsiders have an interest equal to their stock proportion of the net worth of the subsidiary, and this capital liability to outsiders must be shown in the consolidated balance sheet.

When the holding company owns all of the subsidiary stock, the working papers prepared at the date of acquisition eliminate the entire capital stock, surplus and deficit accounts of the subsidiary. If there is a minority interest, it would be wrong to eliminate the capital stock and surplus or deficit accounts of the subsidiary entirely, because they represent two things: (1) The capital liability to the holding company, which is an inter-company relation and is therefore eliminated; and (2) the capital liability to the minority stockholders, which is an outside relation and must therefore be shown in the consolidated balance sheet.

Outline of illustrations.—Three illustrations will be given in this chapter. In all of them it will be assumed that the balance sheet is prepared at the date of acquisition, that the holding company paid book value for the shares acquired, and that it purchased 90 per cent of the stock of the subsidiary leaving a minority interest outstanding of 10 per cent.

First illustration: subsidiary has no surplus or deficit at the date of acquisition.

Second illustration: subsidiary has a surplus at the date of acquisition.

Third illustration: subsidiary has a deficit at the date of acquisition.

First illustration—Minority interest in capital stock.—In this illustration it is assumed that the subsidiary had a capital stock of $50,000 and no surplus or deficit at the date when the holding company acquired 90 per cent of its stock, paying

exactly book value therefor, or $45,000. The balance sheets of holding company A and subsidiary B are indicated in the first two columns of the working papers, and are therefore not set out as separate statements.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Cash	$65,000	$60,000		$125,000
Investment in Stock of Co. B (90%)	45,000		45,000	
	$110,000	$60,000	$45,000	$125,000
Liabilities				
Accounts Payable	$20,000	$10,000		$30,000
Capital Stock:				
Co. A	75,000			75,000
Co. B		50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus—Co. A	15,000			15,000
	$110,000	$60,000	$45,000	$125,000

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$125,000	Accounts Payable	$30,000
		Minority Interest—Co. B(10%)	5,000
		Capital Stock	75,000
		Surplus	15,000
	$125,000		$125,000

Second illustration—Minority interest in capital stock plus surplus.—In this illustration it is assumed that the subsidiary had a capital stock of $50,000 and a surplus of $10,000, making a total book value of $60,000 at the date when the holding company acquired 90 per cent of the stock, paying book value therefor, or $54,000. The subsidiary capital stock and surplus accounts represent capital liabilities to the holding company and the minority, as follows:

	Total	*Inter-Co. (90%)*	*Minority (10%)*
Capital Stock	$50,000	$45,000	$5,000
Plus Surplus	10,000	9,000	1,000
Total	$60,000	$54,000	$6,000

In the following working papers, 90 per cent of the stock and surplus are eliminated as an inter-company liability, and the 10 per cent minority interest is extended to the consolidated balance sheet columns as an outside capital liability.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$54,000		$54,000	
Cash.....	46,000	$75,000		$121,000
	$100,000	$75,000	$54,000	$121,000
Liabilities				
Accounts Payable.....	$10,000	$15,000		$25,000
Capital Stock:				
Co. A.....	75,000			75,000
Co. B.....		50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus:				
Co. A.....	15,000			15,000S
Co. B.....		10,000		
Eliminate holding company's 90%			9,000	
Minority interest 10%				1,000M
	$100,000	$75,000	$54,000	$121,000

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash.....	$121,000	Accounts Payable....	$25,000
		Minority Interest in Co. B(10%)	
		Capital Stock..... $5,000	
		Surplus..... 1,000	6,000
		Capital:	
		Capital Stock..... $75,000	
		Surplus..... 15,000	90,000
	$121,000		$121,000

The minority interest may be shown in detail as to capital stock and surplus, as in the foregoing balance sheet, or shown in one amount as in the following balance sheet.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash.....	$121,000	Accounts Payable....	$25,000
		Minority Interest in Co. B (10%)	6,000
		Capital:	
		Capital Stock..... $75,000	
		Surplus..... 15,000	90,000
	$121,000		$121,000

Third illustration—Minority interest in capital stock less deficit.—In this illustration it is assumed that the subsidiary had a capital stock of $50,000 and a deficit of $10,000, making a net worth of $40,000 at the time when the holding company acquired 90 per cent of its stock, paying book value therefor, or $36,000. The subsidiary's capital stock and deficit accounts represent capital liabilities to the holding company and the minority as follows:

	Total	*Inter-Co.* (90%)	*Minority* (10%)
Capital Stock.....	$50,000	$45,000	$5,000
Less Deficit.....	10,000	9,000	1,000
Net.....	$40,000	$36,000	$4,000

In the following working papers, 90 per cent of the subsidiary's stock and deficit are eliminated as an inter-company liability, and 10 per cent of these accounts are extended to the consolidated balance sheet columns as an outside capital liability.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$36,000		$36,000	
Cash.....	64,000	$55,000		$119,000
Deficit—Co. B.....		10,000		
Eliminate holding company's 90%.			9,000	
Minority interest 10%.				1,000M
	$100,000	$65,000	$45,000	$120,000
Liabilities				
Accounts Payable.....	$10,000	$15,000		$25,000
Capital Stock:				
Co. A.....	75,000			75,000
Co. B.....		50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus—Co. A.....	15,000			15,000S
	$100,000	$65,000	$45,000	$120,000

In the following consolidated balance sheet, the minority interest is shown as $4,000, which is their 10 per cent of the capital stock minus their 10 per cent of the deficit.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$119,000	Accounts Payable		$25,000
		Minority Interest in Co. B (10%)		4,000
		Capital:		
		Capital Stock	$75,000	
		Surplus	15,000	90,000
	$119,000			$119,000

CHAPTER V

GOODWILL

Purchase price in excess of book value.—In all preceding illustrations the holding company has paid exactly book value for the subsidiary stock. In this chapter we shall consider the effect on the consolidated balance sheet in case the holding company pays more than book value.

When the holding company pays more than book value for the subsidiary stock, the balance of the investment account no longer represents merely the holding company's interest in the subsidiary's net assets. The purchase price is now composed of two elements; a payment equal to the book value of the interest acquired in the subsidiary's net assets, and a premium paid to obtain the interest. The treatment to be given to this premium may be made clearer by considering how a similar premium would be dealt with in the case of a merger.

Treatment in a merger.—Let us assume that Company B has the following balance sheet:

BALANCE SHEET—COMPANY B

Machinery	$25,000	Accounts Payable	$15,000
Inventory	30,000	Capital Stock	50,000
Cash	10,000		
	$65,000		$65,000

Company A has the following balance sheet:

BALANCE SHEET—COMPANY A

Cash	$75,000	Capital Stock	$75,000

Company A wishes to obtain control of Company B. To do so it may adopt either the merger procedure, purchasing the assets and assuming the liabilities, or the holding company procedure, purchasing the stock. The price agreed upon is $55,000, which is $5,000 in excess of the book value of Company B.

If the merger procedure is adopted, Company A's entries will be:

Machinery		$25,000	
Inventory		30,000	
Cash		10,000	
Goodwill		5,000	
Accounts Payable			$15,000
Company B, Vendor			55,000
To record the purchase of the assets and the assumption of the liabilities of Company B.			
Purchase price	$55,000		
Assets per Co. B's books	$65,000		
Less liabilities assumed	15,000		
Net assets per Co. B's books	50,000		
Excess payment charged to goodwill	$ 5,000		
Company B, Vendor		$55,000	
Cash			$55,000
To record the payment of cash for the net assets and goodwill of Company B.			

Company A's balance sheet after the purchase will be as follows:

BALANCE SHEET—COMPANY A

Machinery	$25,000	Accounts Payable	$15,000
Inventory	30,000	Capital Stock	75,000
Cash	30,000		
Goodwill	5,000		
	$90,000		$90,000

Treatment in a holding company.—If the holding company procedure is adopted, Company A will make the following entry:

Investment in Stock of Company B		$55,000	
Cash			$55,000
To record the purchase of the entire outstanding stock of Company B.			
Purchase price	$55,000		
Book value of stock acquired	50,000		
Payment in excess of book value	$5,000		

In preparing the consolidated balance sheet, the investment account is replaced by the things which it represents. When

the holding company pays exactly book value, the investment account represents the net assets on the subsidiary's books; when the holding company pays more than book value, the investment account represents two things: (1) the book value of the subsidiary's net assets, and (2) the excess payment, which is goodwill.

Therefore, in the consolidated working papers that portion of the investment account which represents subsidiary net assets is eliminated; and the portion which represents excess payment is carried out to the consolidated balance sheet column, and appears in the consolidated balance sheet as goodwill.

Outline of illustrations.—Six illustrations will be given in this chapter, divided into two groups. In all of the illustrations the purchase price will be in excess of the book value of the subsidiary stock at the date of acquisition; and in all of the illustrations the consolidated balance sheet will be prepared at the date of acquisition.

Group I. Holding company acquires 100 per cent interest.
- First illustration: Subsidiary has no surplus or deficit.
- Second illustration: Subsidiary has a surplus.
- Third illustration: Subsidiary has a deficit.

Group II. Holding company acquires a 90 per cent interest.
- Fourth illustration: Subsidiary has no surplus or deficit.
- Fifth illustration: Subsidiary has a surplus.
- Sixth illustration: Subsidiary has a deficit.

In all of these illustrations the following principles, already explained, will govern the eliminations:

Investment account: Eliminate the book value of the stock acquired, carrying out any excess as goodwill.

Subsidiary capital stock, surplus and deficit accounts: Eliminate the holding company's proportion as an inter-company relation, carrying out the minority's interest.

First illustration.—In this illustration it will be assumed that at the date of acquisition the subsidiary has a capital stock of $50,000 and no surplus or deficit. The holding company acquires all of the stock, paying $57,000 therefor.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (100%)..	$57,000			
Eliminate book value:				
Capital stock			$50,000	
Goodwill				$ 7,000 C
Cash	43,000	$60,000		103,000
	$100,000	$60,000	$50,000	$110,000
Liabilities				
Accounts Payable	$10,000	$10,000		$20,000
Capital Stock:				
Co. A	75,000			75,000
Co. B		50,000		
Eliminate holding company's 100%			$50,000	
Surplus—Co. A	15,000			15,000
	$100,000	$60,000	$50,000	$110,000

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$103,000	Accounts Payable	$ 20,000
Goodwill	7,000	Capital Stock	75,000
		Surplus	15,000
	$110,000		$110,000

Second illustration.—In this illustration it will be assumed that at the date of acquisition, the subsidiary has a capital stock of $50,000 and a surplus of $10,000, making a total book value of $60,000. The holding company acquires all of the stock, paying $63,000 therefor.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (100%)..	$ 63,000			
Eliminate book value:				
Capital Stock			$50,000	
Surplus			10,000	
Goodwill				$ 3,000 G
Cash	37,000	$65,000		102,000
	$100,000	$65,000	$60,000	$105,000

Liabilities	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Accounts Payable	$10,000	$5,000		$15,000
Capital Stock:				
Co. A	75,000			75,000
Co. B		50,000		
Eliminate holding company's 100%			$50,000	
Surplus:				
Co. A	15,000			15,000
Co. B		10,000		
Eliminate holding company's 100%			10,000	
	$100,000	$65,000	$60,000	$105,000

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$102,000	Accounts Payable	$15,000
Goodwill	3,000	Capital Stock	75,000
		Surplus	15,000
	$105,000		$105,000

Third illustration.—In this illustration it will be assumed that at the date of acquisition the subsidiary has a capital stock of $50,000 and a deficit of $10,000, making the net book value of the stock $40,000. The holding company acquires all of the stock, paying $42,000 therefor.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (100%)..	$42,000			
Eliminate book value:				
Capital Stock			$50,000	
Less Deficit			10,000*	
Goodwill				$ 2,000 G
Cash	58,000	$45,000		103,000
Deficit—Co. B		10,000		
Eliminate holding company's 100%			10,000	
	$100,000	$55,000	$50,000	$105,000
Liabilities				
Accounts Payable	$15,000	$5,000		$20,000
Capital Stock:				
Co. A	75,000			75,000
Co. B		50,000		
Eliminate holding company's 100%			$50,000	
Surplus—Co. A	10,000			10,000
	$100,000	$55,000	$50,000	$105,000

*Indicates a deduction.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$103,000	Accounts Payable	$20,000
Goodwill	2,000	Capital Stock	75,000
		Surplus	10,000
	$105,000		$105,000

Fourth illustration.—In this illustration it will be assumed that at the date of acquisition the subsidiary has a capital stock of $50,000 and no surplus. The holding company acquires a 90 per cent interest, the book value of which is $45,000 and the purchase price $48,000.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$48,000			
Eliminate book value:				
Capital stock: 90% of $50,000			$45,000	
Goodwill				$ 3,000 G
Cash	52,000	$65,000		117,000
	$100,000	$65,000	$45,000	$120,000
Liabilities				
Accounts Payable	$10,000	$15,000		$25,000
Capital Stock:				
Co. A	75,000			75,000
Co. B		50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus—Co. A	15,000			15,000
	$100,000	$65,000	$45,000	$120,000

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$117,000	Accounts Payable	$25,000
Goodwill	3,000	Minority Interest in Co. B (10%)	5,000
		Capital Stock	75,000
		Surplus	15,000
	$120,000		$120,000

Fifth illustration.—In this illustration it will be assumed that at the date of acquisition the subsidiary has a capital stock of $50,000 and a surplus of $10,000, making a total book value of $60,000. The holding company acquires a 90 per cent interest, the book value of which is $54,000 and the purchase price $57,000.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$57,000			
Eliminate book value:				
Capital stock: 90% of $50,000			$45,000	
Surplus : 90% of 10,000			9,000	
Goodwill				$ 3,000G
Cash	43,000	75,000		118,000
	$100,000	$75,000	$54,000	$121,000
Liabilities				
Accounts Payable	$10,000	$15,000		$25,000
Capital Stock:				
Co. A	75,000			75,000
Co. B		50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus:				
Co. A	15,000			15,000
Co. B		10,000		
Eliminate holding company's 90%			9,000	
Minority interest 10%				1,000M
	$100,000	$75,000	$54,000	$121,000

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$118,000	Accounts Payable	$25,000
Goodwill	3,000	Minority Interest—Co. B (10%)	6,000
		Capital Stock	75,000
		Surplus	15,000
	$121,000		$121,000

Sixth illustration.—In this illustration it will be assumed that at the date of acquisition the subsidiary has a capital stock of

$50,000 and a deficit of $10,000, making a net book value of $40,000. The holding company acquires a 90 per cent interest, the book value of which is $36,000, and the purchase price $38,000.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$38,000			
Eliminate book value:				
Capital Stock: 90% of $50,000...			$45,000	
Less Deficit: 90% of 10,000...			9,000*	
Goodwill				$ 2,000 G
Cash	62,000	$55,000		117,000
Deficit—Co. B		10,000		
Eliminate holding company's 90%			9,000	
Minority interest 10%				1,000M
	$100,000	$65,000	$45,000	$120,000
Liabilities				
Accounts Payable	$10,000	$15,000		$25,000
Capital Stock:				
Co. A	75,000			75,000
Co. B		50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus—Co. A	15,000			15,000
	$100,000	$65,000	$45,000	$120,000

* Indicates a deduction.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$117,000	Accounts Payable	$25,000
Goodwill	2,000	Minority Interest—Co. B (10%)	4,000
		Capital Stock	75,000
		Surplus	15,000
	$119,000		$119,000

Summary.—It will be noted that in all of these illustrations:

1. The excess of the purchase price over the book value of the acquired stock at the date of acquisition appears on the consolidated balance sheet as goodwill.

2. The minority interest is its stock proportion of the subsidiary's capital stock plus its proportion of the subsidiary's surplus or minus its proportion of the subsidiary's deficit.
3. The holding company's surplus at the date of acquisition is not affected by the fact that the subsidiary's books show either a surplus or a deficit.

On the consolidated balance sheet the excess of purchase price over book value at acquisition will not appear as a separate item of goodwill, but will be added to any goodwill accounts on the books of the related companies, the total being shown as one item.

Chapter VI

DEDUCTION FROM GOODWILL

Book value in excess of purchase price.—If the subsidiary has a goodwill account at the date when the holding company acquires its stock interest, and if the holding company pays less than book value for the stock, the presumption is that the holding company does not recognize the goodwill as conservatively valued and is therefore unwilling to pay book value for the stock. Therefore, when the purchase price is less than the book value of the stock as shown on the subsidiary's books, the deficiency should be deducted from any goodwill appearing on the subsidiary's books. Only the net amount of goodwill thus ascertained will appear on the consolidated balance sheet.

Cases may arise when the holding company pays less than book value and there is no goodwill on the subsidiary's books; the consideration of these cases will be deferred until a subsequent chapter.

Outline of illustrations.—Six illustrations will be given in this chapter, divided into two groups. In all of the illustrations the purchase price will be less than book value, there will be a goodwill account on the subsidiary's books, and the consolidated balance sheet will be prepared at the date of acquisition.

Group I. Holding company acquires a 100 per cent interest.
- First illustration: subsidiary has no surplus or deficit.
- Second illustration: subsidiary has a surplus.
- Third illustration: subsidiary has a deficit.

Group II. Holding company acquires a 90 per cent interest.
- Fourth illustration: subsidiary has no surplus or deficit.
- Fifth illustration: subsidiary has a surplus.
- Sixth illustration: subsidiary has a deficit.

In all of these illustrations, the principles already discussed will govern the eliminations:

Investment account: eliminate the book value of the stock acquired, the excess of the book value eliminated over the

cost of the stock being carried to the consolidated balance sheet column as a negative figure to be deducted from the subsidiary's goodwill.

Subsidiary's capital stock, surplus and deficit accounts: eliminate the holding company's proportion as an inter-company relation, carrying out the minority's interest.

First illustration.—In this illustration it is assumed that at the date of acquisition the subsidiary has a capital stock of $50,000 and no surplus or deficit. The holding company acquires all of the stock, paying $49,000 therefor, or $1,000 less than the book value.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*	
Investment in Stock of Co. B (100%)	$49,000				
Eliminate book value:					
Capital Stock			$50,000		
Deduction from goodwill				$ 1,000*	G
Goodwill		3,000		3,000	G
Cash	51,000	57,000		108,000	
	$100,000	$60,000	$50,000	$110,000	
Liabilities					
Accounts Payable	$15,000	$10,000		$25,000	
Capital Stock:					
Co. A	75,000			75,000	
Co. B		50,000			
Eliminate holding company's 100%			50,000		
Surplus—Co. A	10,000			10,000	
	$100,000	$60,000	$50,000	$110,000	

*Indicates deduction.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$108,000	Accounts Payable	$25,000
Goodwill	2,000	Capital Stock	75,000
		Surplus	10,000
	$110,000		$110,000

Second illustration.—In this illustration it is assumed that at the date of acquisition the subsidiary has a capital stock of $50,000 and a surplus of $10,000, making a total book value of $60,000. The holding company acquires all of the stock, paying $59,000 therefor, or $1,000 less than book value.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (100%).	$59,000			
Eliminate book value:				
Capital Stock			$50,000	
Surplus			10,000	
Deduction from goodwill				$1,000* G
Cash	41,000	$61,000		102,000
Goodwill		4,000		4,000 G
	$100,000	$65,000	$60,000	$105,000
Liabilities				
Accounts Payable	$10,000	$5,000		$15,000
Capital Stock:				
Co. A	75,000			75,000
Co. B		50,000		
Eliminate holding company's 100%			$50,000	
Surplus:				
Co. A	15,000			15,000
Co. B		10,000		
Eliminate holding company's 100%			10,000	
	$100,000	$65,000	$60,000	$105,000

* Indicates a deduction.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$102,000	Accounts Payable	$15,000
Goodwill	3,000	Capital Stock	75,000
		Surplus	15,000
	$105,000		$105,000

Third illustration.—In this illustration it is assumed that at the date of acquisition the subsidiary has a capital stock of $50,000 and a deficit of $10,000, making a net book value of

$40,000. The holding company acquires all of the stock, paying $39,000 therefor, which is $1,000 less than book value.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (100%).	$39,000			
Eliminate book value:				
Capital Stock			$50,000	
Deficit			10,000*	
Deduction from goodwill				$ 1,000*G
Cash	61,000	$42,000		103,000
Goodwill		3,000		3,000G
Deficit—Co. B		10,000		
Eliminate holding company's 100%			10,000	
	$100,000	$55,000	$50,000	$105,000
Liabilities				
Accounts Payable	$15,000	$5,000		$20,000
Capital Stock:				
Co. A	75,000			75,000
Co. B		50,000		
Eliminate holding company's 100%			$50,000	
Surplus—Co. A	10,000			10,000
	$100,000	$55,000	$50,000	$105,000

* Indicates a deduction.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash	$103,000	Accounts Payable	$20,000
Goodwill	2,000	Capital Stock	75,000
		Surplus	10,000
	$105,000		$105,000

Fourth illustration.—In this illustration it is assumed that at the date of acquisition the subsidiary has a capital stock of $50,000 and no surplus. Its book value is therefore $50,000. The holding company acquires a 90 per cent interest, the book value of which is $45,000. The purchase price was $44,000, or $1,000 less than book value.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*	
Investment in Stock of Co. B (90%)..	$44,000				
Eliminate book value:					
Capital stock: 90% of $50,000..			$45,000		
Deduction from goodwill.....				$1,000*	G
Cash.....	56,000	62,000		118,000	
Goodwill.....		3,000		3,000	G
	$100,000	$65,000	$45,000	$120,000	
Liabilities					
Accounts Payable.....	$10,000	$15,000		$25,000	
Capital Stock:					
Co. A.....	75,000			75,000	
Co. B.....		50,000			
Eliminate holding company's 90%			$45,000		
Minority interest 10%				5,000	M
Surplus—Co. A.....	15,000			15,000	
	$100,000	$65,000	$45,000	$120,000	

* Indicates a deduction.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash.....	$118,000	Accounts Payable.....	$25,000
Goodwill	2,000	Minority Interest—Co. B (10%)	5,000
		Capital Stock.....	75,000
		Surplus.....	15,000
	$120,000		$120,000

Fifth illustration.—In this illustration it is assumed that at the date of acquisition the subsidiary has a capital stock of $50,000 and a surplus of $10,000, making a total book value of $60,000. The holding company acquires a 90 per cent interest, the book value of which is $54,000 and the purchase price $53,000.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*	
Investment in Stock of Co. B (90%)..	$53,000				
Eliminate book value:					
Capital stock: 90% of $50,000..			$45,000		
Surplus: 90% of 10,000..			9,000		
Deduction from goodwill.....				$ 1,000*	G
Cash.....	47,000	72,000		119,000	
Goodwill.....		3,000		3,000	G
	$100,000	$75,000	$54,000	$121,000	
Liabilities					
Accounts Payable.....	$10,000	$15,000		$25,000	
Capital Stock:					
Co. A.....	75,000			75,000	
Co. B.....		50,000			
Eliminate holding company's 90%			$45,000		
Minority interest 10%				5,000	M
Surplus:					
Co. A.....	15,000			15,000	
Co. B.....		10,000			
Eliminate holding company's 90%			9,000		
Minority interest 10%				1,000	M
	$100,000	$75,000	$54,000	$121,000	

* Indicates a deduction.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash.....	$119,000	Accounts Payable.....	$25,000
Goodwill.....	2,000	Minority Interest—Co. B (10%)	6,000
		Capital Stock.....	75,000
		Surplus.....	15,000
	$121,000		$121,000

Sixth illustration.—In this illustration it is assumed that at the date of acquisition the subsidiary has a capital stock of $50,000 and a deficit of $10,000, making a net book value of $40,000. The holding company acquires a 90 per cent interest, the book value of which is $36,000 and the purchase price $35,000.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*	
Investment in Stock of Co. B (90%)...	$35,000				
Eliminate book value:..					
Capital Stock: 90% of $50,000..			$45,000		
Deficit: 90% of 10,000..			9,000*		
Deduction from goodwill.....				$ 1,000*	G
Cash.....	65,000	$52,000		117,000	
Goodwill.....		3,000		3,000	G
Deficit—Co. B.....		10,000			
Eliminate holding company's 90%			9,000		
Minority interest 10%				1,000	M
	$100,000	$65,000	$45,000	$120,000	
Liabilities					
Accounts Payable.....	$10,000	$15,000		$25,000	
Capital Stock:					
Co. A.....	75,000			75,000	
Co. B.....		50,000			
Eliminate holding company's 90%			$45,000		
Minority interest 10%				5,000	M
Surplus—Co. A.....	15,000			15,000	
	$100,000	$65,000	$45,000	$120,000	

* Indicates a deduction.

COMPANY A AND SUBSIDIARY B

CONSOLIDATED BALANCE SHEET

(Date)

Cash.....	$117,000	Accounts Payable.....	$25,000
Goodwill.....	2,000	Minority Interest—Co. B (10%)	4,000
		Capital Stock.....	75,000
		Surplus.....	15,000
	$119,000		$119,000

Summary of the first six chapters.—In all of the illustrations thus far presented the consolidated balance sheet has been prepared at the date of acquisition, and the following principles and procedure have been found to apply:

1. All similar assets and liabilities are combined.
2. The investment account is not shown in the consolidated balance sheet; the book value of the subsidiary stock is eliminated; any excess of purchase price over book value is carried to the consolidated balance sheet as goodwill; any excess of the book value over the purchase price is deducted from the goodwill on the subsidiary's books.
3. The subsidiary's capital stock, surplus and deficit accounts are entirely eliminated if the holding company owns all of the subsidiary stock; if it owns only a controlling interest each of these accounts is divided into two parts: (a) the holding company's proportion, which is eliminated; and (b) the minority's interest, which is shown on the consolidated balance sheet.

In later chapters we shall consider the procedure of making eliminations when the consolidated balance sheet is prepared at a date subsequent to the date of acquisition, after the subsidiary has made profits or losses and paid dividends. Before considering these cases, however, it is necessary to describe the approved method for the holding company to record its share of subsidiary profits, losses and dividends. This will be done in the next chapter.

Chapter VII

SUBSIDIARY'S PROFITS, LOSSES AND DIVIDENDS ON THE HOLDING COMPANY'S BOOKS

Subsidiary profits.—If the subsidiary makes a profit after the holding company acquires its stock, this profit increases the net assets of the subsidiary and correspondingly increases the value of the stock owned by the holding company. Hence, after the subsidiary has closed its books and ascertained its profits, the holding company should take up its share of these profits by debiting the investment account and crediting an account with some title such as Income from Subsidiary. This account is closed into Profit and Loss or Surplus. It will be noted that the holding company takes up its share of the profits and increases its investment account as soon as the subsidiary ascertains its profits; this practice is justified because the two companies are so closely related that the profits of the subsidiary are virtually profits of the holding company which owns the subsidiary.

Subsidiary losses.—If the subsidiary suffers a loss, the holding company should debit Loss from Subsidiary to take up its share of the loss, and credit the investment account to show the reduction in the value of the stockholdings in the subsidiary.

Subsidiary dividends.—When the subsidiary declares a dividend, the holding company should debit Dividends Receivable and credit the investment account. Since the holding company took up the profits of the subsidiary as income, the dividends do not constitute additional income but are a conversion of the asset of stock investment into a current asset of dividends receivable.

In other words, profits earned by the subsidiary increase the value of the subsidiary stock, and hence are added to the investment account by a debit entry; dividends decrease the net assets of the subsidiary and hence are deducted from the investment account by a credit entry.

When the subsidiary pays the dividend, the holding company should debit Cash and credit Dividends Receivable.

If at the time of the acquisition of the stock, a dividend has been declared by the subsidiary but has not been paid, and if the right to receive the dividend passes to the holding company, the holding company should record the transaction by a debit to Dividends Receivable for the amount of the dividend, and a debit to Investment in Stock for the remainder of the purchase price.

Illustrative journal entries.—The proper method of taking up subsidiary profits, losses and dividends may be illustrated by the following example. Company A acquired the entire issue of the stock of Company B. At the date of acquisition Company B had a capital stock of $100,000 and a surplus of $50,000. The holding company paid $150,000 for the stock.

Investment in Stock of Company B	$150,000	
Cash		$150,000
To record the purchase of the entire issue of Company B's stock.		

Immediately after the holding company acquired the stock, the subsidiary declared a 10 per cent dividend. This dividend was not income to the holding company; the holding company virtually purchased the net assets of the subsidiary when it acquired the stock, and the dividend merely transfers a portion of these assets to the holding company. The dividend was a conversion of a portion of the permanent investment into a current asset.

Dividends Receivable	$10,000	
Investment in Stock of Company B		$10,000
To record the declaration of a dividend by Company B, payable on (date).		

At a later date the subsidiary paid the dividend, and the holding company's asset of dividends receivable was converted into cash.

Cash	$10,000	
Dividends Receivable		$10,000
To record the collection of the dividend from Company B.		

During the first year following the acquisition of the stock, the subsidiary made a profit of $25,000. This was virtually an

earning for the holding company, and it resulted in a $25,000 increase in the value of the subsidiary stock.

Investment in Stock of Company B	$25,000	
Income from Company B		$25,000
To take up our profits arising from the operations of subsidiary Company B.		

The subsidiary then declared and immediately paid a dividend of $5,000. Although this dividend may have been paid from profits earned since the holding company acquired control of the stock, the dividend should not be treated as income because the holding company has already taken up the income for the year. Since the dividend was paid immediately upon declaration, it need not be passed through a Dividends Receivable account but may be recorded as follows:

Cash	$5,000	
Investment in Stock of Company B		$5,000
To record collection of a dividend from Company B.		

During the second year the subsidiary lost $20,000, thus decreasing its net assets and the value of the stock owned by the parent company. The parent company should take up the loss by the following entry:

Loss of Subsidiary B	$20,000	
Investment in Stock of Company B		$20,000
To take up the loss resulting from the year's operations of subsidiary Company B.		

Balance of the investment account.—When the holding company records its share of subsidiary profits, losses and dividends in the manner just described, the balance of the investment account will show at the close of each successive fiscal period:

1. The book value of the subsidiary stockholdings at that date,
2. Plus any goodwill involved in the purchase, due to the fact that the purchase price was in excess of the book value of the acquired stock at the date of acquisition,
3. Or minus any negative goodwill involved in the purchase, due to the fact that the purchase price was less than the book value of the acquired stock at the date of acquisition.

This fact will be demonstrated by a number of illustrations.

First illustration.—This illustration is based on the journal entries shown in the preceding sections of this chapter. The account with the investment on Company A's books will appear as follows:

INVESTMENT IN STOCK OF COMPANY B

Cost	$150,000	Dividends	$10,000
Profits—First year	25,000	Dividends	5,000
		Loss—Second year	20,000

The balance of the account is $140,000.
The subsidiary's surplus at this date is:

Opening balance		$50,000
Minus first dividend		10,000
		$40,000
Plus first year's profits		25,000
		$65,000
Minus second dividend		5,000
		$60,000
Minus second year's loss		20,000
Present surplus		$40,000

Hence the present book value of the subsidiary is $140,000. Thus the balance of the investment account at this date is equal to the book value of the stock held; there is no goodwill nor negative goodwill, for the holding company paid exactly book value.

Second illustration.—The subsidiary Company B has a capital stock of $100,000 and at the date when the holding company acquired its stock the subsidiary had a surplus of $50,000. The holding company purchased a 90 per cent interest, which had a book value of 90 per cent of $150,000, or $135,000. The price paid was $138,000; hence there was a $3,000 goodwill element in the stock purchase. During the first two years after the holding company acquired the stock the subsidiary's surplus account exhibited the following changes:

	Debits	*Credits*
Balance at date of holding company's acquisition		$50,000
Profits—first year		10,000
Dividend—first year	$ 6,000	
Loss—second year	3,000	
Balance at the present date	51,000	
	$60,000	$60,000

The subsidiary's book value is now $151,000, and 90 per cent thereof is $135,900.

The investment account on the holding company's books will appear as follows:

INVESTMENT IN STOCK OF COMPANY B

Cost	$138,000	Dividend—first year	$ 5,400
Profits—first year	9,000	Loss—second year	2,700
		Balance at present date	138,900
	$147,000		$147,000
This balance of			$138,900
Represents:			
The present book value of 90% of the subsidiary stock			135,900
and the goodwill (as computed above)			$3,000

Third illustration.—The subsidiary Company B has a capital stock of $100,000, and at the date when the holding company acquired its stock it had a deficit of $15,000. The holding company purchased a 90 per cent interest, which had a book value of 90 per cent of $85,000, or $76,500. The price paid was $73,000; hence there was a negative goodwill of $3,500 in the stock purchase. During the first two years after the holding company acquired its stock, the subsidiary's surplus account exhibited changes as follows:

	Debits	*Credits*
Balance at date of holding company's acquisition	$15,000	
Profits—first year		$35,000
Dividends—first year	5,000	
Loss—second year	3,000	
Balance at the present date	12,000	
	$35,000	$35,000

The subsidiary's book value is now $112,000, and 90 per cent thereof is $100,800. The investment account on the holding company's books will appear as follows:

INVESTMENT IN STOCK OF COMPANY B

Cost	$73,000	Dividends—first year	$ 4,500
Profits—first year	31,500	Loss—second year	2,700
		Balance at the present date	97,300
	$104,500		$104,500
This balance of			$97,300
Represents:			
The present book value of 90% of the subsidiary stock.			$100,800
Minus the negative goodwill (as computed above)			3,500
			$97,300

Chapter VIII

BALANCE SHEETS AFTER DATE OF ACQUISITION

Function of working papers.—Consolidated balance sheet working papers are prepared in order to accomplish the following objects:

1. Combine the assets and liabilities of a similar nature.
2. Determine any goodwill or negative goodwill involved in the stock purchase.
3. Ascertain the minority interest in the stock and surplus of the subsidiary.
4. Show the capital stock and surplus of the holding company.

The preceding chapters have shown how these objects are accomplished when the consolidated balance sheet is prepared at the date of acquisition. It is the purpose of this chapter to show how the necessary facts are ascertained when the balance sheet is prepared at a date subsequent to acquisition, and when the holding company carries its investment account in the manner described in the preceding chapter.

The assets and liabilities of a similar nature are combined in the manner already described, regardless of the date of the balance sheet, and this subject requires no further discussion.

Goodwill or negative goodwill.—In the preceding chapter it was shown that when the holding company follows the approved method of accounting, the investment account at any date has a balance equal to the book value of the stock held, plus any goodwill or minus any negative goodwill arising from the stock purchase. Therefore the goodwill element can be ascertained by eliminating the book value of the subsidiary holdings at the date of the balance sheet; a positive remainder is an addition to the goodwill, and a negative remainder is a deduction from the goodwill.

Minority interest.—The minority interest is its stock proportion of the subsidiary's capital stock and surplus at the date of the balance sheet. This interest is ascertained by eliminating the holding company's proportion of these accounts, and

carrying out the minority's interest. The reader is already familiar with this procedure.

Holding company's capital stock and surplus.—The entire outstanding capital stock of the holding company as well as its surplus is carried to the consolidated balance sheet. This surplus account contains not only the gains and losses arising from the holding company's own operations, but also the proportion of the subsidiary's gains and losses accruing to the holding company. If the investment account has been carried in the approved manner, these gains and losses have been taken up on the holding company's books.

Summary of eliminations.—From the preceding paragraphs it will be noted that the following eliminations are made:

On the asset side:—From the investment account: eliminate the present book value of the stock held, represented by the par of the stock and the proportion of subsidiary surplus applicable thereto. A positive remainder is goodwill; a negative remainder is a deduction from goodwill.

On the liability side:—From the subsidiary capital stock: eliminate the par of the stock held by the parent company, carrying out the remainder as minority interest.

From the subsidiary surplus: eliminate the surplus applicable to the stock owned by the parent company, carrying out the remainder as minority interest.

Outline of illustrations.—Nine illustrations will be given in this chapter, designed to show the method of preparing consolidated balance sheet working papers under a variety of conditions. They will be divided into three groups, as follows:

First group: 100 per cent interest; no goodwill; no subsidiary surplus at date of acquisition.

- First illustration: at date of acquisition; no subsidiary surplus.
- Second illustration: at end of first year; subsidiary surplus.
- Third illustration: at end of two years; subsidiary deficit.

Second Group: 90 per cent interest; goodwill; subsidiary surplus at acquisition.

- Fourth illustration: at date of acquisition; subsidiary surplus.
- Fifth illustration: at end of one year; subsidiary surplus increased.
- Sixth illustration: at end of two years; subsidiary deficit.

Third Group: 90 per cent interest; negative goodwill; subsidiary deficit at acquisition.

- Seventh illustration: at date of acquisition; subsidiary deficit.
- Eighth illustration: at end of one year; subsidiary deficit increased.
- Ninth illustration: at end of two years; subsidiary surplus.

The sundry assets and liabilities will be omitted, as they are not essential to show the method of making eliminations of inter-company accounts.

In all of the illustrations it will be assumed that the holding company made no profits or losses other than those accruing from its ownership of the subsidiary stock.

First illustration.—Working papers prepared at the date of acquisition.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (100%)..	$50,000			
Eliminate present book value:				
Capital stock.....			$50,000	
Liabilities				
Capital Stock:				
Co. A.....	$75,000			$75,000
Co. B.....		$50,000		
Eliminate holding company's 100%			$50,000	
Surplus:—Co. A.....	15,000			15,000

Second illustration.—During the year the subsidiary has made a profit of $12,000, and hence it has a surplus of that amount. The holding company has taken up this profit, thus raising its investment account to $62,000 and its surplus to $27,000.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (100%)..	$62,000			
Eliminate present book value:				
Capital Stock.....			$50,000	
Surplus.....			12,000	
Liabilities				
Capital Stock:				
Co. A.....	$75,000			$75,000
Co. B.....		$50,000		
Eliminate holding company's 100%			$50,000	
Surplus:				
Co. A.....	27,000			27,000
Co. B.....		12,000		
Eliminate holding company's 100%			12,000	

Third illustration.—During the second year the subsidiary lost $18,000, thus wiping out its surplus and leaving it with a deficit of $6,000. The holding company took up the loss, reducing its investment account to $44,000, and its surplus to $9,000.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (100%)..	$44,000			
Eliminate present book value:				
Capital Stock			$50,000	
Deficit			6,000*	
Deficit—Co. B		$6,000		
Eliminate holding company's 100%			6,000	
Liabilities				
Capital Stock:				
Co. A	$75,000			$75,000
Co. B		$50,000		
Eliminate holding company's 100%			$50,000	
Surplus—Co. A	9,000			9,000

Fourth illustration.—The subsidiary had a capital stock of $50,000 and a surplus of $10,000 at the date when the holding company acquired its stock. The holding company purchased 90 per cent of the stock, the book value of which was $54,000, and the purchase price $56,000. The working papers are prepared at the date of acquisition.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)..	$56,000			
Eliminate present book value:				
Capital stock: 90% of 50,000			$45,000	
Surplus: 90% of 10,000			9,000	
Goodwill				$2,000 G
Liabilities				
Capital Stock:				
Co. A	$75,000			$ 75,000
Co. B		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus:				
Co. A	15,000			15,000
Co. B		10,000		
Eliminate holding company's 90%			9,000	
Minority interest 10%				1,000M

Fifth illustration.—During the first year the subsidiary made a profit of $4,000, thus increasing its surplus to $14,000. The holding company took up its 90 per cent of this profit,

or $3,600, thus increasing its investment account to $59,600 and its surplus to $18,600.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$59,600			
Eliminate present book value:				
Capital stock: 90% of 50,000			$45,000	
Surplus: 90% of 14,000			12,600	
Goodwill				$2,000 G
Liabilities				
Capital Stock:				
Co. A	$75,000			$75,000
Co. B		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus:				
Co. A	18,600			18,600
Co. B		14,000		
Eliminate holding company's 90%			12,600	
Minority interest 10%				1,400M

Sixth illustration.—During the second year the subsidiary lost $16,000, wiping out its surplus account and leaving it with a deficit of $2,000. The holding company took up 90 per cent of this loss, or $14,400, thus reducing its investment account to $45,200 and its surplus to $4,200.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$45,200			
Eliminate present book value:				
Capital stock: 90% of 50,000			$45,000	
Deficit: 90% of 2,000			1,800*	
Goodwill				$2,000 G
Deficit Co. B		$2,000		
Eliminate holding company's 90%			1,800	
Minority interest 10%				200M
Liabilities				
Capital Stock:				
Co. A	$75,000			$75,000
Co. B		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus—Co. A	4,200			4,200

Seventh illustration.—The subsidiary had a capital stock of $50,000 and a deficit of $10,000 at the date when the holding company acquired its stock. The holding company pur-

chased 90 per cent of the stock, the book value of which was $36,000 and the purchase price $34,000. The working papers are prepared at the date of acquisition.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$34,000			
Eliminate present book value:				
Capital stock: 90% of 50,000....			$45,000	
Deficit: 90% of 10,000....			9,000*	
Deduction from goodwill.....				$2,000*G
Deficit—Co. B.....		$10,000		
Eliminate holding company's 90%			9,000	
Minority interest 10%				1,000 M
Liabilities				
Capital Stock:				
Co. A.....	$75,000			$75,000
Co. B.....		$50,000		
Eilminate holding company's 90%			$45,000	
Minority interest 10%				5,000 M
Surplus—Co. A.....	2,000			2,000

Eighth illustration.—During the first year the subsidiary lost $5,000, thus increasing its deficit to $15,000. The holding company took up 90 per cent of this loss, or $4,500, thereby reducing its investment account to $29,500, and changing its surplus of $2,000 into a deficit of $2,500.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$29,500			
Eliminate present book value:				
Capital stock: 90% of $50,000...			$45,000	
Deficit: 90% of 15,000...			13,500*	
Deduction from goodwill.....				$2,000*G
Deficit:				
Co. A.....	2,500			2,500
Co. B.....		$15,000		
Eliminate holding company's 90%			13,500	
Minority interest 10%				1,500M
Liabilities				
Capital Stock				
Co. A.....	$75,000			$75,000
Co. B.....		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M

Ninth illustration.—During the second year the subsidiary made a profit of $30,000 and paid a dividend of $5,000, thereby causing a net increase of $25,000 in its surplus, changing its

$15,000 deficit into a $10,000 surplus. The holding company took up its 90 per cent of the profits and its 90 per cent of the dividends, with the following results:

	Investment Account	*Surplus*
Balances at end of first year (as above).....	$29,500	$ 2,500*
Add profits—90% of $30,000.....	27,000	27,000
Balances after adding profits.....	56,500	24,500
Deduct dividend—90% of $5,000.....	4,500	
Balances at end of year.....	52,000	24,500

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)..	$52,000			
Eliminate present book value:				
Capital Stock 90% of 50,000..			45,000	
Surplus 90% of 10,000..			9,000	
Deduction from goodwill.....				$2,000* G
Liabilities				
Capital Stock:				
Co. A.....	$75,000			$75,000
Co. B.....		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000 M
Surplus:				
Co. A.....	24,500			24,500
Co. B.....		10,000		
Eliminate holding company's 90%			9,000	
Minority interest 10%				1,000 M

Summary of illustrations.—In the next chapter the illustrations will be based on the same assumed facts as those in this chapter, and the reader will have occasion to refer to the results obtained in this chapter. These results are therefore summarized here to facilitate reference.

	Goodwill	*Holding Company Surplus*	*Minority Interest*		
			Capital Stock	*Surplus or Deficit**	*Total or Net*
First Group:					
First illustration.....	0	$15,000	0	0	0
Second illustration.....	0	27,000	0	0	0
Third illustration.....	0	9,000	0	0	0
Second Group:					
Fourth illustration.....	$2,000	15,000	$5,000	$1,000	$6,000
Fifth illustration.....	2,000	18,600	5,000	1,400	6,400
Sixth illustration.....	2,000	4,200	5,000	200*	4,800
Third Group:					
Seventh illustration.....	2,000*	2,000	5,000	1,000*	4,000
Eighth illustration.....	2,000*	2,500*	5,000	1,500*	3,500
Ninth illustration.....	2,000*	24,500	5,000	1,000	6,000

Chapter IX

BALANCE SHEETS AFTER DATE OF ACQUISITION

Continued

Investment Account Carried at Cost

Determining the goodwill.—The reader is already familiar with the principle that the goodwill element is the difference between the book value of the stock at the date of acquisition and the purchase price. When the investment account is carried continuously at cost, without entries for subsidiary profits, losses and dividends, the balance of the account represents:

1. The book value at the date of acquisition,
2. Plus any goodwill due to the fact that the purchase price was in excess of book value,
3. Or minus any negative goodwill due to the fact that the purchase price was less than book value.

Therefore, when the investment account is carried at cost, the goodwill element is ascertained by eliminating the book value of the stock *at the date of acquisition;* a positive remainder is an addition to goodwill, and a negative remainder is a deduction from goodwill.

Minority interest.—The minority interest is always the minority's stock proportion of the capital stock and surplus of the subsidiary at the date of the balance sheet. The method used by the holding company in carrying its investment account has no bearing whatever on the computation of the minority interest.

Holding company surplus.—When the holding company takes up the profits and losses of the subsidiary in the manner described in Chapter VII, the holding company's surplus account reflects its portion of the subsidiary's net gain or loss after the date of acquisition. If the holding company does

not take up gains and losses in this manner, its surplus account does not reflect its portion of the net increase or decrease in subsidiary surplus after the date of acquisition. Therefore the holding company's surplus appearing on the consolidated balance sheet must be computed as follows:

1. The holding company's own surplus account,
2. Plus its proportion of the net increase in the subsidiary's surplus since the date of acquisition,
3. Or minus its proportion of the net decrease in the subsidiary's surplus since the date of acquisition.

Summary of eliminations.—From the foregoing discussion it will be apparent that when the holding company carries the investment account at cost, the book value of the subsidiary stock at the date of acquisition is eliminated, instead of the book value at the date of the consolidated balance sheet, as was done in the preceding chapter. The eliminations may be summarized as follows:

On the asset side:—From the investment account: eliminate the book value of the subsidiary stock at the date of acquisition, represented by the par of the stock held and the proportion of the subsidiary's surplus or deficit at that date applicable to the holding company. A positive remainder is an addition to goodwill; a negative remainder is a deduction from goodwill.

On the liability side:—From the subsidiary capital stock: eliminate the par of the stock held by the parent company, carrying out the remainder as minority interest.

From the subsidiary surplus or deficit: eliminate the holding company's proportion thereof at the date of acquisition; carry out the minority's proportion of the present surplus or deficit; and carry out the holding company's proportion of the net increase or decrease in the account since the date of acquisition, this latter item being combined with the holding company's surplus account to obtain the total or net surplus on the consolidated balance sheet.

Outline of illustrations.—The nine illustrations in the preceding chapter will be repeated in this chapter, the only change being the fact that the holding company carries the investment account at cost. After each illustration is completed, the reader should refer to the summary at the close of Chapter VIII and note that the same results are obtained in each corresponding pair of cases.

First illustration.—Working papers prepared at the date of acquisition; the holding company purchased all of the stock of the subsidiary, paying book value therefor. Book value was par, for the subsidiary had no surplus or deficit.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (100%) Cost	$50,000			
Eliminate book value at acquisition:				
Capital stock			$50,000	
Liabilities				
Capital Stock:				
Co. A	$75,000			$75,000
Co. B		$50,000		
Eliminate holding company's 100%			$50,000	
Surplus—Co. A	15,000			15,000 S

There is no goodwill, the holding company's surplus is $15,000, and there is no minority interest.

Second illustration.—During the year the subsidiary made a profit of $12,000, and hence it has a surplus of that amount. The holding company has not taken up this profit; hence its investment account and its surplus remain unchanged.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B(100%)Cost	$50,000			
Eliminate book value at acquisition:				
Capital stock			$50,000	
Liabilities				
Capital Stock:				
Co. A	$75,000			$75,000
Co. B		$50,000		
Eliminate holding company's 100%			$50,000	
Surplus:				
Co. A	15,000			15,000 S
Co. B		12,000		12,000 S

There is no goodwill.

The surplus shown on the consolidated balance sheet will be $27,000, being the sum of the holding company's own surplus account and 100 per cent of the earnings of the subsidiary since the date of acquisition.

There is no minority interest.

Third illustration.—During the second year the subsidiary lost $18,000, thus wiping out its surplus and leaving it with a deficit of $6,000. The holding company made no record of this loss and hence its investment account and its surplus remain unchanged.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B(100%)Cost	$50,000			
Eliminate book value at acquisition:				
Capital stock			$50,000	
Deficit—Co. B		$6,000		
Holding company's 100% of decrease in surplus since the date of acquisition				$6,000 S
Liabilities				
Capital Stock:				
Co. A	$75,000			$75,000
Co. B		$50,000		
Eliminate holding company's 100%			$50,000	
Surplus—Co. A	15,000			15,000 S

There is no goodwill.

The holding company's surplus on the consolidated balance sheet will be shown as $9,000, being the holding company's own surplus balance of $15,000 minus its $6,000 proportion of the net loss of the subsidiary since the date of acquisition.

There is no minority interest.

Fourth illustration.—The subsidiary had a capital stock of $50,000 and a surplus of $10,000 at the date when the holding company acquired its stock. The holding company purchased 90 per cent of the stock, the book value of which was $54,000, and the purchase price $56,000. The balance sheet is made at the date of acquisition.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$56,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $50,000			$45,000	
Surplus: 90% of 10,000			9,000	
Goodwill				$2,000 G
Liabilities				
Capital Stock:				
Co. A	$75,000			$75,000
Co. B		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus:				
Co. A	15,000			15,000 S
Co. B		10,000		
Minority: 10% of present surplus				1,000M
Eliminate holding company's 90%			9,000	

There is a $2,000 addition to goodwill. The holding company's surplus is $15,000. The minority interest is $5,000 capital stock plus $1,000 surplus, or $6,000.

Fifth illustration.—During the first year the subsidiary made a profit of $4,000, thus increasing its surplus to $14,000. The holding company made no entries for this profit; hence its investment account and its surplus remain unchanged.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$56,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $50,000...			$45,000	
Surplus: 90% of 10,000...			9,000	
Goodwill				$2,000 G
Liabilities				
Capital Stock:				
Co. A	$75,000			$75,000
Co. B		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus:				
Co. A	15,000			15,000 S
Co. B		14,000		
Minority: 10% of 14,000				
present surplus				1,400M
Elim. H. C.: 90% of 10,000				
surplus at acquis			9,000	
H. C. Surplus: 90% of 4,000				
increase				3,600 S

There is a $2,000 addition to goodwill.

The holding company's surplus will appear on the consolidated balance sheet at $18,600, being the holding company's surplus account of $15,000 plus $3,600, which is its 90 per cent of the increase in the subsidiary's surplus since acquisition.

The minority interest is $5,000 stock plus $1,400 surplus, or $6,400.

Sixth illustration.—During the second year the subsidiary lost $16,000, wiping out its $14,000 surplus and leaving it with a deficit of $2,000. The holding company made no entry for this loss, and hence its investment account and its surplus remain unchanged.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$56,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $50,000...			$45,000	
Surplus: 90% of 10,000...			9,000	
Goodwill				$2,000 G
Deficit—Co. B		$2,000		
Minority: 10% of $ 2,000				
present deficit				200M
Elim. H. C. 90% of 10,000				
surplus at acquisition...			9,000*	
Surplus: 90% of $12,000				
decrease in surplus				10,800 S
Liabilities				
Capital Stock:				
Co. A	$ 75,000			$75,000
Co. B		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000M
Surplus—Co. A	15,000			15,000 S

There is a $2,000 addition to goodwill.

The holding company's surplus will appear on the consolidated balance sheet at $4,200, being the holding company's surplus account of $15,000 minus $10,800 which is its 90 per cent of the net decrease in the subsidiary's surplus since the date of acquisition.

The minority interest is $5,000 stock minus $200 deficit, or $4,800.

It will be observed that an asterisk appears after the second $9,000 surplus elimination, indicating that this item is to be deducted in obtaining the total of the elimination column. This is because a surplus item is being deducted from a deficit. The asterisk would be used also if a deficit at acquisition were being deducted from a surplus at the date of the balance sheet.

Seventh illustration.—The subsidiary had a capital stock of $50,000 and a deficit of $10,000 at the date when the holding company acquired its stock. The holding company purchased 90 per cent of the stock, the book value of which was $36,000 and the purchase price $34,000. The working papers are prepared at the date of acquisition.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$34,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $50,000...			$45,000	
Deficit: 90% of 10,000...			9,000*	
Deduction from goodwill.....				$2,000*G
Deficit—Co. B.....		$10,000		
Minority: 10% of $10,000 present deficit				1,000 M
Elim. H. C.: 90% of 10,000 deficit at acquisition			9,000	
Liabilities				
Capital Stock:				
Co. A.....	$75,000			$75,000
Co. B.....		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000 M
Surplus—Co. A.....	2,000			2,000 S

There is a $2,000 deduction from goodwill.

The holding company's surplus is $2,000, the balance of its surplus account. The subsidiary has made no gains or losses since the date of acquisition.

The minority interest is $5,000 stock minus $1,000 deficit, or $4,000.

Eighth illustration.—During the first year the subsidiary lost $5,000, thus increasing its deficit to $15,000. The holding company made no entries for this loss; hence its investment account and its surplus remain unchanged.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$34,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $50,000...			$45,000	
Deficit: 90% of 10,000...			9,000*	
Deduction from goodwill.....				$2,000*G
Deficit—Co. B.....		$15,000		
Minority: 10% of $15,000 present deficit				1,500 M
Elim. H. C.: 90% of 10,000 deficit at acquisition			9,0000	
Surplus: 90% of $ 5,000 decrease since				4,500* S
Liabilities				
Capital Stock:				
Co. A.....	$75,000			$75,000
Co. B.....		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000 M
Surplus—Co. A.....	2,000			2,000 S

There is a $2,000 deduction from goodwill.

The deficit appearing on the consolidated balance sheet will be $2,500, being the holding company's surplus of $2,000 minus $4,500 which is its 90 per cent of the $5,000 decrease in subsidiary surplus since the date of acquisition.

The minority interest is $5,000 stock minus $1,500 deficit, or $3,500.

Ninth illustration.—During the second year the subsidiary made a profit of $30,000 and paid a dividend of $5,000, causing a net increase of $25,000 in its surplus, thereby changing its $15,000 deficit into a surplus of $10,000.

The holding company made no entry for its share of the $30,000 profits, but it recorded the collection of its share of the $5,000 dividend by debiting Cash and crediting Surplus with $4,500. This entry causes no change in the investment account, but the holding company's surplus is increased from $2,000 to $6,500.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$34,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $50,000...			$45,000	
Deficit: 90% of 10,000...			9,000*	
Deduction from goodwill.....				$2,000*G
Liabilities				
Capital Stock:				
Co. A.....	$75,000			$75,000
Co. B.....		$50,000		
Eliminate holding company's 90%			$45,000	
Minority interest 10%				5,000 M
Surplus:				
Co. A.....	6,500			6,500 S
Co. B.....		10,000		
Minority: 10% of $10,000 present surplus				1,000 M
Elim. H. C.: 90% of 10,000 deficit at acquisition ..			9,000*	
Surplus: 90% of $20,000 increase since				18,000 S

There is a $2,000 deduction from goodwill.

The surplus appearing on the consolidated balance sheet will be $24,500, being the sum of the holding company's $6,500 surplus account and the $18,000, which is its 90 per cent of the increase in the subsidiary's surplus since the date of acquisition.

Review Exercises

When the holding company takes up its share of subsidiary profits, losses and dividends through the investment account, eliminations are based on the book value of the subsidiary stock at the date of the consolidated balance sheet. When the holding company carries the investment account at cost, eliminations are based on the book value at the date of acquisition.

As a means of reviewing these principles, it is suggested that the reader prepare consolidated balance sheet working papers for the following cases.

In all cases it is assumed that the holding company owns 90 per cent of the subsidiary stock. In each group of eight cases, the first four are based on the assumption that the holding company has taken up its 90 per cent of the subsidiary gains and losses through its investment account; the second four are based on the same subsidiary profits and losses, but the investment account is carried at cost. Neither company has paid any dividends.

To simplify the cases, the various assets and liabilities are shown in a single amount, as sundry net assets. The holding company has no source of income other than its investment in the subsidiary stock.

The solution to the first case is given to illustrate the form:

Case A:

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90)%	$110,000			
Eliminate present book value:				
Capital stock: 90% of $100,000			$90,000	
Surplus: 90% of 20,000			18,000	
Goodwill				$ 2,000 G
Sundry Net Assets	105,000	$120,000		225,000
	$215,000	$120,000	$108,000	$227,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A	15,000			15,000 S
Co. B		20,000		
Eliminate holding company's 90%			18,000	
Minority interest 10%				2,000M
	$215,000	$120,000	$108,000	$227,000

		COMPANY A—BALANCE SHEET			COMPANY B—BALANCE SHEET		
		Investment Account	*Sundry Net Assets*	*Capital Stock*	*Surplus*	*Sundry Net Assets*	*Capital Stock*	*Surplus*
Group I:								
Case A	At acquisition	$110,000	$105,000	$200,000	$15,000	$120,000	$100,000	$20,000
Case B	End of 1 year B gain $10,000	119,000	105,000	200,000	24,000	130,000	100,000	30,000
Case C	End of 2 years B loss 15,000	105,500	105,000	200,000	10,500	115,000	100,000	15,000
Case D	End of 3 years B loss 25,000	83,000	105,000	200,000	12,000*	90,000	100,000	10,000*
Case AA	At acquisition	110,000	105,000	200,000	15,000	120,000	100,000	20,000
Case BB	End of 1 year	110,000	105,000	200,000	15,000	130,000	100,000	30,000
Case CC	End of 2 years	110,000	105,000	200,000	15,000	115,000	100,000	15,000
Case DD	End of 3 years	110,000	105,000	200,000	15,000	90,000	100,000	10,000*
Group II:								
Case E	At acquisition	115,000	100,000	200,000	15,000	120,000	100,000	20,000
Case F	End of 1 year B gain $20,000	133,000	100,000	200,000	33,000	140,000	100,000	40,000
Case G	End of 2 years B loss 28,000	107,800	100,000	200,000	7,800	112,000	100,000	12,000
Case H	End of 3 years B loss 20,000	89,800	100,000	200,000	10,200*	92,000	100,000	8,000*
Case EE	At acquisition	115,000	100,000	200,000	15,000	120,000	100,000	20,000
Case FF	End of 1 year	115,000	100,000	200,000	15,000	140,000	100,000	40,000
Case GG	End of 2 years	115,000	100,000	200,000	15,000	112,000	100,000	12,000
Case HH	End of 3 years	115,000	100,000	200,000	15,000	92,000	100,000	8,000*

* Deficit

		COMPANY A—BALANCE SHEET				COMPANY B—BALANCE SHEET		
		Investment Account	*Sundry Net Assets*	*Capital Stock*	*Surplus*	*Sundry Net Assets*	*Capital Stock*	*Surplus*
Group III:								
Case I	At acquisition	$105,000	$80,000	$200,000	$15,000*	$120,000	$100,000	$20,000
Case J	End of 1 year B gain $20,000	123,000	80,000	200,000	3,000	140,000	100,000	40,000
Case K	End of 2 years B loss 28,000	97,800	80,000	200,000	22,200*	112,000	100,000	12,000
Case L	End of 3 years B loss 20,000	79,800	80,000	200,000	40,200*	92,000	100,000	8,000*
Case II	At acquisition	105,000	80,000	200,000	15,000*	120,000	100,000	20,000
Case JJ	End of 1 year	105,000	80,000	200,000	15,000*	140,000	100,000	40,000
Case KK	End of 2 years	105,000	80,000	200,000	15,000*	112,000	100,000	12,000
Case LL	End of 3 years	105,000	80,000	200,000	15,000*	92,000	100,000	8,000*
Group IV:								
Case M	At acquisition	85,000	130,000	200,000	15,000	90,000	100,000	10,000*
Case N	End of 1 year B gain $ 8,000	92,200	130,000	200,000	22,200	98,000	100,000	2,000*
Case O	End of 2 years B gain 14,000	104,800	130,000	200,000	34,800	112,000	100,000	12,000
Case P	End of 3 years B loss 30,000	77,800	130,000	200,000	7,800	82,000	100,000	18,000*
Case MM	At acquisition	85,000	130,000	200,000	15,000	90,000	100,000	10,000*
Case NN	End of 1 year	85,000	130,000	200,000	15,000	98,000	100,000	2,000*
Case OO	End of 2 years	85,000	130,000	200,000	15,000	112,000	100,000	12,000
Case PP	End of 3 years	85,000	130,000	200,000	15,000	82,000	100,000	18,000*
Group V:								
Case Q	At acquisition	80,000	105,000	200,000	15,000*	90,000	100,000	10,000*
Case R	End of 1 year B gain $ 8,000	87,200	105,000	200,000	7,800*	98,000	100,000	2,000*
Case S	End of 2 years B gain 14,000	99,800	105,000	200,000	4,800	112,000	100,000	12,000
Case T	End of 3 years B loss 30,000	72,800	105,000	200,000	22,200*	82,000	100,000	18,000*
Case QQ	At acquisition	80,000	105,000	200,000	15,000*	90,000	100,000	10,000*
Case RR	End of 1 year	80,000	105,000	200,000	15,000*	98,000	100,000	2,000*
Case SS	End of 2 years	80,000	105,000	200,000	15,000*	112,000	100,000	12,000
Case TT	End of 3 years	80,000	105,000	200,000	15,000*	82,000	100,000	18,000*

* Deficit.

Chapter X

INTER-COMPANY RECEIVABLES AND PAYABLES

Current accounts.—It has already been stated that the object of the consolidated balance sheet is to show the financial condition of a group of related companies in relation to the outside world. In doing so, all inter-company accounts are eliminated.

Related companies frequently buy from and sell to each other on credit, with the result that the accounts receivable of one company will include a balance due from a related company; and the same inter-company relation will be recorded among the accounts payable of the other company. In preparing the consolidated balance sheet working papers, the inter-company accounts receivable and accounts payable must be eliminated, only the net amounts being carried to the balance sheet columns. These net amounts will represent the accounts receivable due from the outside world and the accounts payable due to the outside world.

Advances.—When the capital of one company is inadequate to its needs, one of the other related companies may advance funds to it. The company receiving the advance will credit it to Advances from ——— Company, and the company making the advance will charge it to Advances to ——— Company. These two accounts represent an inter-company relation, to be offset in the elimination columns.

Notes receivable.—If the inter-company indebtedness takes the form of a note, one company will have an account Notes Receivable—Company ———, and the other company will have an account Notes Payable—Company ———. These two accounts should also be offset in the elimination columns.

Notes receivable discounted.—The situation is a little more complex when one company has discounted notes receivable taken from another company. To illustrate, let it be assumed that Company A has given a $5,000 note to Company B. Company B has discounted this note with its bankers. At the date of the consolidated balance sheet, the note has not

matured; therefore the following accounts will appear in the trial balances of the two companies:

COMPANY A		
Notes Payable—Company B		$5,000
COMPANY B		
Notes Receivable—Company A	$5,000	
Notes Receivable—Company A—Discounted		5,000

Since the note is in the hands of the bankers, the liability is no longer an inter-company one, and hence it must be shown as a liability on the consolidated balance sheet. The Notes Payable account on Company A's books should be offset against the Notes Receivable account on Company B's books, and the Notes Receivable—Company A—Discounted account should be carried to the consolidated balance sheet column, thus:

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Notes Receivable—Co. A		$5,000	$5,000	
Liabilities				
Notes Payable—Co. B	$5,000		$5,000	
Notes Rec.—Co. A—Discounted		5,000		$5,000

There is a difference of opinion among accountants as to whether the $5,000 liability to the outside world should be shown in the consolidated balance sheet as Notes Receivable—Company A—Discounted, or as Notes Payable. Those who favor the former title contend that the note is a direct liability of one of the related companies and a secondary liability of the other company and hence is an obligation different in nature from a note signed by one company only. Showing the liability as a note payable would not indicate the liability of both companies.

The author's opinion is that the Notes Payable title is preferable. In the first place, the consolidated balance sheet is based on the assumption that the related companies are a single organization, the legal fact of separate corporate entities being ignored. From the viewpoint of the consolidated balance sheet, therefore, a note signed by one company is as much a liability of the organization as a note signed by one company and endorsed by another related company. In the second place, the term Notes Receivable Discounted at once suggests a contingent liability, and since an inter-company note discounted with an outsider is a positive liability, the term is likely to be misleading.

Inter-company bond holdings.—When one company holds bonds of another company, the bonds held as an asset by one company may be offset against the bond liability of the other company, and only the net amount outstanding in the hands of the public be shown as a liability. It is preferable, however, to carry out the asset account and the liability account to the balance sheet columns of the working papers, and deduct the inter-company holdings from the total liability on the face of the consolidated balance sheet.

If a corporation has an authorized bond issue of $500,000, of which only $400,000 has been issued, the facts should be shown on its balance sheet thus:

Bonds Payable—Authorized	$500,000	
Less Treasury Bonds	100,000	
Bonds Outstanding		$400,000

This procedure is followed because the mortgage is security for the full issue of $500,000, and the company has $100,000 of bonds available for issue or for use as collateral for short term loans on notes payable.

The situation is analogous in the case of inter-company bond holdings, as the bonds are virtually treasury bonds of the organization, available for issue or for use as collateral.

Premium or discount on inter-company bond holdings.—If the company which purchased the bonds paid more than par for them, it may have written off the premium against its surplus immediately. It is better accounting, however, to amortize the premium by periodical charges to interest. When this is done the balance of the bond investment account at all times prior to maturity will be in excess of the par of the bonds. In preparing the consolidated working papers, the bond account should be divided into two parts, par and premium. The portion representing par should be handled in the manner described in the preceding section, and the portion representing premium should be carried to the consolidated balance sheet as unamortized premium on the purchase of treasury bonds under the caption of deferred charges. Thus:

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Bonds of Co. B	$27,500			
Par (Shown on the C. B. S. as treasury bonds)				$27,000
Unamortized premium (Shown as a deferred charge)				500

If the company bought the bonds at a discount, the working papers should be prepared as follows:

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Bonds of Co. B	$26,700			
Par				$27,000
Unamortized discount				300*

The unamortized discount should be shown on the consolidated balance sheet under the caption of deferred credits.

Accrued interest.—If there are inter-company bonds or notes, the balance sheet of the company issuing the paper may show a liability for accrued interest. The company holding the paper should then show an asset of accrued interest receivable. The accrued interest receivable should be offset against the accrued interest payable, only the net amount due to the outside creditors being shown on the consolidated balance sheet.

Declared dividends unpaid.—If the subsidiary has declared dividends which are unpaid at the date of the balance sheet, its books will show a liability of dividends payable. The holding company's books should show an asset of dividends receivable, which should be offset against the dividends payable. The consolidated balance sheet will then show only the dividends declared and payable to the outside or minority stockholders.

Adjusting inter-company accounts.—All inter-company relations should be shown on the books of both related companies, so that the same amount may be eliminated from the assets and the liabilities. If any inter-company transactions have been recorded on the books of one company only, they should be taken up on the books of the other company before the consolidated balance sheet is prepared.

Goods may have been sold by one company to another just prior to the close of the year and recorded in the current account of the selling company, but not taken up in the books of the purchasing company. Before preparing the consolidated balance sheet these goods should be added to the purchasing company's inventory and credited to the purchasing company's current account with the selling company.

If services have been rendered by one company and recorded by a charge to the current account and a credit to income, and if the balance sheet of the other company is drawn up before recording the transaction, an adjustment should be made

debiting Surplus and crediting the current account of the company rendering the service.

If a company holding bonds of a related company has not taken up its share of the accrued interest on these bonds, an adjustment should be made debiting Bond Interest Receivable and crediting Surplus.

If the subsidiary has declared a dividend which is unpaid at the date of the balance sheet and which is shown on its books as Dividends Payable, the holding company should take up its share by a debit to Dividends Receivable. The offsetting credit will depend upon the method adopted by the holding company for carrying its investment in the subsidiary stock. If it has taken up its share of subsidiary profits and losses by the method explained in Chapter VII, the offsetting credit for the dividend will be made in the investment account. If the investment account is carried at cost, the offsetting credit will be made to Surplus.

All of these adjustments may be indicated by the use of Adjustment columns in the consolidated working papers.

Illustration.—Company A owns 90 per cent of the stock of Company B and 95 per cent of the stock of Company C. It carries its investment account with Company C at cost, but has taken up its share of the profits and losses of Company B. The balance sheets of the three companies at December 31, 1921, were as follows:

BALANCE SHEET—COMPANY A

Investment in Stock of Co. B	$64,000	Accounts Payable	$ 25,000
Investment in Stock of Co. C	68,000	Capital Stock	100,000
Cash	5,000	Surplus	69,000
Co. B Current	6,000		
Advances to Co. C	10,000		
Investment in Bonds of Co. B	41,000		
	$194,000		$194,000

BALANCE SHEET—COMPANY B

Cash	$20,000	Bonds Payable	$50,000
Merchandise Inventory	40,000	Bond Interest Accrued	1,500
Notes Receivable—Co. C	15,000	Accounts Payable	15,000
Plant	75,000	Company A Current	8,000
		Notes Receivable—Co. C—Discounted	6,000
		Dividends Payable	3,000
		Capital Stock	50,000
		Surplus	16,500
	$150,000		$150,000

BALANCE SHEET—COMPANY C

Cash	$ 3,000	Accounts Payable	$ 5,000
Merchandise Inventory	62,000	Advances from Co. A	10,000
Notes Receivable	11,000	Notes Payable—Co. B	15,000
Plant	14,000	Dividends Payable	2,000
		Capital Stock	40,000
		Surplus	18,000
	$90,000		$90,000

Company A holds bonds of Company B of a par value of $40,000; the additional $1,000 in the bond investment account represents unamortized premium. At the date when Company A acquired its interest in the stock of Company C, the latter company had a surplus of $30,000. The Company B Current account in the holding company's balance sheet has a balance of $6,000, while the offsetting current account on Company B's balance sheet has a balance of $8,000. This difference is accounted for as follows: Company A acts as a selling agent for Company B on a commission basis, and at December 31 Company A charged Company B $1,000 as commission on sales made during December, and these commissions have not been taken up on the books of Company B. On December 30 Company B drew a draft on Company A for $3,000, depositing the proceeds; this transaction has not been taken up on the books of Company A. The holding company has not taken up its proportion of accrued bond interest and declared dividends.

Explanation of adjustments.—Capital letters are used to indicate offsetting adjustments and small letters to indicate offsetting eliminations. Adjustments are made as follows:

(A) To take up the holding company's 90 per cent of the dividends declared by Company B. Ninety per cent of $3,000 = $2,700. Since the holding company has reflected its share of the profits and losses of Company B in its investment account, the dividends declared should be treated as a reduction of the investment account. Hence the entry: debit Dividends Receivable and credit Investment in Stock of Company B.

(B) To take up on the holding company's records the draft drawn by Company B, by a debit to Company B Current and a credit to Cash, $3,000.

(C) To take up the interest accrued on bonds of Company B held by Company A; debit Bond Interest Receivable and credit Surplus $1,200, being 80 per cent of the $1,500 accrued bond interest shown in Company B's balance sheet.

(D) To take up the holding company's 95 per cent of the dividends declared by Company C. Ninety-five per cent of $2,000 = $1,900. Since the holding company is carrying its investment in Company C stock at cost, the dividends are treated as income. Hence the entry: debit Dividends Receivable and credit Surplus.

(E) To take up on Company B's records the commission charged by Company A on sales, $1,000. Debit Surplus and credit Company A Current. This entry affects the surplus of Company B and hence the amount eliminated from the Company B investment account on Company A's balance sheet.

COMPANY A AND SUBSIDIARY COMPANIES B AND C

CONSOLIDATED BALANCE SHEET

December 31, 1921

	Assets		
Current Assets:			
Cash		$25,000	
Notes Receivable		11,000	
Merchandise Inventory		102,000	$138,000
Fixed Assets:			
Plant		89,000	
Goodwill		3,850	92,850
Deferred Charges:			
Unamortized Premium on Purchase of Treasury Bonds			1,000
			$231,850
	Liabilities		
Current Liabilities:			
Accounts Payable		$45,000	
Notes Payable		6,000	
Accrued Bond Interest		300	
Dividends Payable		400	$51,700
Fixed Liabilities:			
Bonds Payable		50,000	
Less Treasury Bonds		40,000	10,000
Minority Interests:			
Company B—10%		6,550	
Company C— 5%		2,900	9,450
Capital:			
Capital Stock		100,000	
Surplus		60,700	160,700
			$231,850

COMPANY A AND SUBSIDIARY COMPANIES B AND C

Consolidated Balance Sheet—Working Papers

December 31, 1921

Assets	*Co. A*	*Co. B*	*Co. C*	*Adjustments Dr.*	*Adjustments Cr.*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$64,000				$2,700(A)		
Eliminate present book value:							
Capital stock: 90% of $50,000						$45,000(a)	
Surplus: 90% of 15,500						13,950(b)	
Goodwill							$2,350 G
Investment in Stock of Co. C (95%) Cost	68,000						
Eliminate book value at date of acquisition:							
Capital stock: 95% of $40,000						38,000(c)	
Surplus: 95% of 30,000						28,500(d)	
Goodwill							1,500 G
Cash	5,000	$20,000	$3,000		3,000(B)		25,000
Co. B Current	6,000			$3,000(B)		9,000(e)	
Advances to Co. C	10,000					10,000(f)	
Investment in Bonds of Co. B	41,000						40,000
Par of bonds							1,000
Unamortized premium							102,000
Merchandise Inventory		40,000	62,000			15,000(g)	
Notes Receivable—Co. C		15,000					89,000
Plant		75,000	14,000				11,000
Notes Receivable			11,000				
Bond Interest Receivable (On 40,000 Co. B bonds)				1,200(C)		1,200(h)	
Dividends Receivable:							
Co. B stock: 90% of $3,000				2,700(A)		2,700(i)	
Co. C stock: 95% of 2,000				1,900(D)		1,900(j)	
	$194,000	$150,000	$90,000	$8,800	$5,700	$165,250	$271,850

Liabilities	*Co. A*	*Co. B*	*Co. C*	*Adjustments Dr.*	*Adjustments Cr.*	*Elim.*	*C. B. S.*
Adjustment column totals—forward.				$8,800	$5,700		
Accounts Payable	$25,000	$15,000	$5,000				$45,000
Bond Interest Accrued		1,500				$1,200(h)	300
Company A Current		8,000			1,000(E)	9,000(e)	
Notes Receivable—Company C—Discounted		6,000					6,000
Dividends Payable:							
Co. B		3,000				2,700(i)	300
Co. C			2,000			1,900(j)	100
Bonds Payable		50,000					50,000
Advances from Company A			10,000			10,000(f)	
Notes Payable—Co. B			15,000			15,000(g)	
Capital Stock:							
Co. A	100,000						100,000
Co. B		50,000					
Eliminate holding company's 90%						45,000(a)	
Minority interest 10%							5,000M
Co. C			40,000				
Eliminate holding company's 95%						38,000(c)	
Minority interest 5%							2,000M
Surplus:							
Co. A	69,000						
Add bond interest accrued					1,200(C)		
Add dividends on Co. C stock					1,900(D)		
Co. B		16,500					72,100 S
Deduct commissions				1,000(E)			
Minority 10% of $15,500 present surplus							1,550M
Elim. H. C. 90% of 15,500 present surplus						13,950(b)	
Co. C			18,000				
Minority 5% of $18,000 present surplus							900M
Elim. H. C. 95% of 30,000 surplus at acquisition						28,500(d)	
Surplus 95% of 12,000 decrease							11,400*S
	$194,000	$150,000	$90,000	$9,800	$9,800	$165,250	$271,850

Chapter XI

MISCELLANEOUS TOPICS

Book value at acquisition in excess of cost.—Chapter VI contained a discussion of the treatment of the excess of book value at acquisition over the cost of the stock purchased by the holding company. The discussion in that chapter was limited to the condition where a goodwill account appeared on the books of the subsidiary whose stock was purchased at less than book value. It is now necessary to discuss the proper treatment when the subsidiary has no goodwill account.

It is the custom in such cases to treat the excess of book value over cost as a deduction from goodwill wherever found in the consolidated working papers. That is to say, it may be deducted from goodwill appearing on the books of the holding company, on the books of any other subsidiary, or arising from the purchase of the stock of some other subsidiary at more than book value. While this is customary, it does not seem to be theoretically correct.

Assuming that the subsidiary has no goodwill account at the date of acquisition, the fact that the holding company acquired its stock at less than book value would seem to indicate one of two things: either some asset on the subsidiary's books was over-valued or the holding company made a fortunate purchase, acquiring the right to more net assets than it parted with. If some asset was over-valued, the excess of the book value over purchase price should be deducted on the consolidated balance sheet from the over-valued asset. If no subsidiary asset was over-valued, and if the holding company acquired the subsidiary stock by an issue of its own stock, it would seem that the excess value received over the par of the stock issued in payment is paid-in surplus, to be shown on the consolidated balance sheet as surplus, set apart as capital surplus if the distinction is desired. If the holding company acquired the subsidiary stock by a cash payment, the excess would still appear to be a proper addition to capital surplus.

It is difficult to see the logic of offsetting "negative goodwill" against goodwill appearing on the holding company's books. If the holding company's goodwill account is a legitimate one, the purchase of a subsidiary's stock at less than book value would not seem to cause a decrease in the value of the holding company's goodwill, unless the subsidiary's earnings were so small that the investment would not pay a reasonable rate of income. In this case the excess earnings of the holding company may be reduced and the capitalized value of the holding company's excess earnings, or goodwill, may be reduced. The same reasoning would apply to offsetting "negative goodwill" against goodwill appearing on the books of one of the other subsidiaries, or against goodwill arising from the purchase of the stock of another subsidiary.

Of course it must be admitted that it is more conservative to deduct such items from goodwill wherever found than to add them to surplus. But it may be said that while it is conservative to write off any goodwill account it is not obligatory to do so. Each case must be decided in the light of all related facts with the guidance of the following principles:

If the subsidiary whose stock is acquired at less than book value has a goodwill account, the negative goodwill should be offset against the subsidiary's goodwill.

If there are over-valued assets on the subsidiary's books, the excess of book value of the stock acquired over cost should be deducted from the assets known to be over-valued. If no specific over-valuation is known, but such over-valuation is believed to exist, the excess cannot be deducted from specific assets but may be shown on the liability side of the consolidated balance sheet as a reserve. Any descriptive title is satisfactory, such as Reserve for Revaluation of Subsidiary Assets.

If no subsidiary assets are over-valued, the excess is a proper addition to the consolidated surplus, preferably shown as Capital Surplus to indicate that it did not arise from operations.

If it is desired to be conservative and write off goodwill accounts, the excess may be deducted from goodwill wherever found.

Minority interest—subsidiary deficit.—In all working papers thus far prepared, the minority interest has been shown at an amount equal to the minority's share of the subsidiary's stock plus its share of the subsidiary's surplus or minus its share of the subsidiary's deficit at the date of the consolidated balance

sheet. In case the subsidiary has a deficit some accountants show the minority interest at the par of the stock without deduction of their pro-rata share of the deficit. The result of this treatment is that the minority's share of the subsidiary's deficit is deducted from the holding company's surplus. The difference in treatment may be shown by the following illustration, in which it is assumed that the holding company has taken up its share of subsidiary gains and losses. In the following working papers the minority interest is reduced by its share of the subsidiary's deficit.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$ 38,000			
Eliminate book value:				
Capital stock: 90% of $50,000			$45,000	
Deficit: 90% of 10,000			9,000*	
Goodwill				$ 2,000 G
Cash	22,000	$20,000		42,000
Merchandise	80,000	45,000		125,000
Deficit—Co. B		10,000		
Minority: 10% of $10,000				1,000M
Elim. H. C.: 90% of 10,000			9,000	
	$140,000	$75,000	$45,000	$170,000
Liabilities				
Accounts Payable	$ 15,000	$25,000		$ 40,000
Capital Stock:				
Co. A	100,000			100,000
Co. B		50,000		
Minority: 10%				5,000M
Elim. H. C.: 90%			$45,000	
Surplus—Co. A	25,000			25,000 S
	$140,000	$75,000	$45,000	$170,000

The minority interest would be shown on the consolidated balance sheet at $4,000, and the holding company's surplus at $25,000.

If the minority's interest is not to be diminished by its share of the subsidiary's deficit, the working papers would be prepared in exactly the same manner, except that the $1,000 portion of the subsidiary's deficit carried out above as a deduction from the minority's interest, would be carried out as a deduction from the holding company's surplus, with the result that the minority interest would be shown at $5,000, the par

of the stock held by the minority, and the holding company's surplus would be shown at $24,000.

Accountants who follow this latter method do so on the theory that while the minority will share in profits, the holding company will be obliged to "absorb the losses" of the subsidiary in order to hold the organization together.

While it is true that the subsidiary may be such an essential part of the organization that the holding company will consider it expedient to retain its ownership of the stock in spite of these losses, it does not seem necessary for the holding company to assume the magnanimous position of allowing the minority to share in subsidiary profits while relieving them from any reduction in the book value of their stock caused by losses. As long as the subsidiary is able to pay its debts the losses merely reduce the value of all shares proportionately. If it comes to a point where the subsidiary is unable to pay its debts it may be necessary for the holding company to advance the funds necessary to pay the debts and prevent the creditors from forcing the subsidiary into liquidation.

As an extreme illustration, let us assume that the subsidiary losses have resulted in a deficit equal to the capital stock, and that the holding company has not seen fit to make advances to keep the business out of the hands of the creditors. The creditors therefore take possession, and the holding company loses its stock and the minority stockholders lose theirs. But the holding company does not bear the minority's loss.

On the other hand, assume that the holding company has made advances, so that the condition is as follows:

SUBSIDIARY BALANCE SHEET

Net Assets	$ 50,000	Advances from Holding Company	$ 50,000
Deficit	100,000	Capital Stock	100,000

The holding company may now take over the assets of the subsidiary in settlement of the advances; again the holding company will lose its share of the stock and the minority will lose their share.

The purpose of a balance sheet is to show the present financial condition of a business organization. It would seem that a consolidated balance sheet fulfils this purpose if it shows all of the assets and liabilities of the combined companies, and the actual present interests of the holding company and the minority's stockholders in these net assets. Regardless of

what the holding company may have to do in the future (and it is difficult to see how it will have to bear more than its share of the loss), it cannot be denied that the present book value of the minority's interest in the net assets of the organization is measured by the minority's share of the subsidiary's capital stock and surplus or deficit.

Stock acquired from the subsidiary.—In all illustrations heretofore presented, it has been assumed that the holding company acquired its stock by purchase from former stockholders of the subsidiary. The stock may be acquired by direct subscription to the subsidiary. The difference in the method of acquiring the stock would have no effect, however, on the method of making eliminations from the investment account. If the investment account has been charged with subsidiary profits and credited with subsidiary losses and dividends, the book value of the stock at the date of the balance sheet should be eliminated; if the investment is carried at cost, the book value at the date of acquisition should be eliminated.

Of course, the book value at the date of acquisition is the book value after the holding company has paid for the stock. To illustrate, a company has an issue of $30,000 of stock, all outstanding in the hands of individual owners. The surplus is $10,000. An additional issue of $70,000 is authorized and sold to a holding company at 150, or $105,000. Eliminations would be made as follows in the working papers prepared at the date of acquisition:

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (70%)...	$105,000			
Eliminate book value:				
Capital stock.....			$70,000	
Surplus: 70% of $45,000.....			31,500	
Goodwill.....				$3,500 G

The $45,000 surplus is the sum of the $10,000 surplus on the books of the subsidiary before the holding company acquired its stock, and the $35,000 premium paid for the stock.

Liabilities	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Capital Stock—Co. B.....		$100,000		
Eliminate holding company's 70%.			$70,000	
Minority 30%.				$30,000M
Surplus—Co. B.....		45,000		
Eliminate holding company's 70%.			31,500	
Minority 30%.				13,500M

Before the issue of additional stock, the old stockholders had a capital interest of $40,000. After the additional issue these stockholders become the minority and have an interest of $43,500. In other words, the holding company paid $3,500 as goodwill to obtain control of this business, and this payment inures to the benefit of the minority stockholders.

Subscription rights.—Corporations frequently allow their stockholders to subscribe for additional stock at par or at some other figure less than book value. Regardless of the price paid for the new stock the transaction has no effect on the goodwill appearing in the consolidated balance sheet, provided all stockholders, including the minority, take new stock at the same price and in amounts proportionate to their former holdings. To illustrate, assume that immediately after the holding company (in the preceding illustration) acquired its stock, the directors of the subsidiary authorized the issue of an additional $50,000 of stock to be subscribed and paid for at par by the present stockholders in proportion to their present holdings. All stock is issued on this basis, the holding company taking $35,000 and the minority $15,000. The working papers follow:

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (70%)...	$140,000			
Eliminate book value:				
Capital stock: 70% of $150,000..			$105,000	
Surplus: 70% of 45,000..			31,500	
Goodwill.....				$3,500 G
Liabilities				
Capital Stock—Co. B.....		$150,000		
Eliminate holding company's 70%.			$105,000	
Minority 30%.				$45,000M
Surplus—Co. B.....		45,000		
Eliminate holding company's 70%.			31,500	
Minority 30%.				13,500M

This illustration shows that when all stockholders pay for new stock at the same price and take it in proportion to their original holdings, their payments to the corporation increase the book value of their holdings an amount exactly equal to their payments and hence there is no effect on the goodwill arising from the original purchase.

If the holding company or the minority should fail to take new stock in amounts exactly proportionate to their former holdings, the computation of the goodwill would be affected

because of the change in the proportion of stock ownership and the consequent change in the interests of the holding company and the minority in the surplus of the subsidiary. This fact may be illustrated by assuming that, in the preceding illustration, the holding company took all of the stock to which it was entitled while the minority stockholders took only $5,000 of new shares. The total issue would be:

	Par		
Stock owned by holding company:			
Original purchase	$70,000		
Additional	35,000	$105,000	75%
Stock owned by minority:			
Original holding	30,000		
Additional	5,000	35,000	25%
		$140,000	100%

CONSOLIDATED WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (75%)	$140,000			
Eliminate book value:				
Capital stock: 75% of $140,000			$105,000	..
Surplus: 75% of 45,000			33,750	
Goodwill				$1,250 G
Liabilities				
Capital Stock—Co. B		$140,000		
Eliminate holding company's 75%			$105,000	
Minority 25%				$35,000M
Surplus—Co. B		45,000		
Eliminate holding company's 75%			33,750	
Minority 25%				11,250M

It will be noted that the minority's interest in the surplus is reduced $2,250 and the holding company's interest therein increased an equal amount. The elimination of this excess amount reduces the goodwill $2,250. It might be contended with very good reason that the original stock purchase and the subsequent subscription are entirely distinct transactions; that the original purchase involved a payment of $3,500 for goodwill, and that the subsequent transaction transferred $2,250 of the subsidiary surplus from the minority to the holding company without cost to the holding company; and

that therefore the goodwill should be shown as $3,500 since this amount was paid for, and that the $2,250 should be added to the holding company's surplus. While this position can be defended, the treatment shown in the working papers is more conservative.

Holdings of no par value stock.—The method of making eliminations is not affected by the fact that the subsidiary's stock has no par value. The book value of the holding company's ownings is determined by ascertaining the per cent of subsidiary stock owned and by eliminating this percentage of the subsidiary's stock and surplus accounts. To illustrate, assume that the subsidiary has an issue of 3,000 shares of no par value stock for which $250,000 has been paid in and credited to Capital Stock. The subsidiary also has a surplus of $60,000. The holding company acquired 2,400 shares for which it pays $260,000.

CONSOLIDATED WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (80%)...				
2,400 shares of a total issue of 3,000	$260,000			
Eliminate book value:				
Capital stock: 80% of $250,000			$200,000	
Surplus: 80% of 60,000			48,000	
Goodwill				12,000 G
Liabilities				
Capital Stock—Co. B		$250,000		
Eliminate holding company's 80%			$200,000	
Minority 20%				$50,000M
Surplus—Co. B		60,000		
Eliminate holding company's 80%			48,000	
Minority 20%				12,000M

Holdings of both common and preferred stock.—When the holding company owns both common and preferred stock, it may be necessary to make a division of the subsidiary surplus into the portions applicable to the two classes of stock, in order to determine their book value and make proper eliminations.

If the holding company owns the same proportion of each class, it will not be necessary to make a division of the subsidiary surplus, since the two investments may be treated as one, and a single elimination made to determine the goodwill. The following working papers are illustrative.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Preferred Stock of Co. B (90%)	$60,000			
Investment in Common Stock of Co. B (90%)	125,000			
Eliminate book value:				
90% of Preferred stock			$45,000	
90% of Common stock			90,000	
90% of Surplus			36,000	
Goodwill				$14,000 G
Liabilities				
Capital Stock Preferred—Co. B		$50,000		
Eliminate holding company's 90%			$45,000	
Minority 10%				$5,000M
Capital Stock Common—Co. B		100,000		
Eliminate holding company's 90%			90,000	
Minority 10%				10,000M
Surplus—Co. B		40,000		
Eliminate holding company's 90%			36,000	
Minority 10%				4,000M

If the holding company owns different proportions of the common and preferred stock, it is necessary to make a division of the subsidiary surplus, and in making this division it is necessary to consider whether the subsidiary's preferred stock is cumulative or non-cumulative, participating or non-participating, and whether there are any cumulative dividends in arrears. In the following illustrations, it will be assumed that the holding company bought 80 per cent of the preferred stock for $48,000 (par value $40,000) and 90 per cent of the common stock for $106,000 (par value $90,000). The subsidiary had no surplus at the date of acquisition. The total paid for goodwill was therefore $8,000 + $16,000, or $24,000. At the end of one year the subsidiary has made a profit of $18,000.

In the first place it will be assumed that the preferred stock is non-cumulative and non-participating, and that the year's dividend of $3,000 has been paid on the preferred stock. The preferred therefore has no further claim on the surplus of the subsidiary, which is reduced to $15,000 by the payment of the preferred dividend, and the entire $15,000 would be applicable to the common stock. Ninety per cent of this amount is $13,500 and this amount should have been taken up by the holding company as well as their $2,400 dividend on the preferred stock.

CONSOLIDATED WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Preferred Stock of Co. B (80%)	$48,000			
Eliminate book value:				
Capital stock: 80% of $50,000			$40,000	
Goodwill				$8,000 G
Investment in Common Stock of Co. B (90%)	119,500			
Eliminate book value:				
Capital stock: 90% of $100,000			90,000	
Surplus: 90% of 15,000			13,500	
Goodwill				16,000 G
Liabilities				
Capital Stock Preferred—Co. B		$50,000		
Eliminate holding company's 80%			$40,000	
Minority 20%				$10,000M
Capital Stock Common—Co. B		100,000		
Eliminate holding company's 90%			90,000	
Minority 10%				10,000M
Surplus—Co. B—Applicable to common stock		15,000		
Eliminate holding company's 90%			13,500	
Minority 10%				1,500M
Surplus—Co. A	15,900			15,900 S

In the second place it will be assumed that the preferred stock is cumulative and non-participating, and that there are no dividends in arrears. The rights of the preferred stockholders in the subsidiary surplus have therefore been satisfied by the payment of the dividend, and the entire surplus is applicable to the common stock. Therefore the working papers would be identical with those just shown.

In the third place it will be assumed that the preferred stock is cumulative but non-participating, and that one year's dividend of 6 per cent is in arrears. The surplus is therefore $18,000. As the profits have been earned, the preferred stockholders have a lien against them to the extent of $3,000, and the holding company would be justified in taking up their 80 per cent thereof by a debit to the investment account and a credit to earnings. The subsidiary surplus is divided into two parts: $3,000 applicable to preferred stock, and $15,000 applicable to common stock.

CONSOLIDATED WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Preferred Stock of Co. B (80%)	$50,400			
Eliminate book value:				
Capital stock: 80% of $50,000			$40,000	
Surplus: 80% of 3,000			2,400	
Goodwill				$8,000 G
Investment in Common Stock of Co. B (90%)	119,500			
Eliminate book value:				
Capital stock: 90% of $100,000			90,000	
Surplus: 90% of 15,000			13,500	
Goodwill				16,000 G
Liabilities				
Capital Stock—Preferred—Co. B		$50,000		
Eliminate holding company's 80%			$40,000	
Minority 20%				$10,000M
Capital Stock—Common—Co. B		100,000		
Eliminate holding company's 90%			90,000	
Minority 10%				10,000M
Surplus—Co. B (Applicable to preferred stock)		3,000		
Eliminate holding company's 80%			2,400	
Minority 20%				600M
Surplus—Co. B (Applicable to common stock)		15,000		
Eliminate holding company's 90%			13,500	
Minority 10%				1,500M
Surplus—Co. A (2,400 + 13,500)	15,900			$15,900 S

In the fourth place it will be assumed that the preferred stock is cumulative and participating and that no dividends have been paid on either preferred or common stock. Since the preferred stock is participating, it shares pro-rata with the common stock in the surplus. Therefore $6,000 of the earnings are applicable to preferred and $12,000 are applicable to common. The holding company would be justified in making the following entry:

Investment in Preferred Stock of Co. B (80% of $6,000)	$ 4,800	
Investment in Common Stock of Co. B (90% of $12,000)	10,800	
Surplus		$15,600

To take up our share of the earnings of Co. B.

CONSOLIDATED WORKING PAPERS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Preferred Stock of Co. B (80%)	$52,800			
Eliminate book value:				
Capital stock: 80% of $50,000			$40,000	
Surplus: 80% of 6,000			4,800	
Goodwill				8,000 G
Investment in Common Stock of Co. B (90%)	116,800			
Eliminate book value:				
Capital stock: 90% of $100,000			90,000	
Surplus: 90% of 12,000			10,800	
Goodwill				16,000 G
Liabilities				
Capital Stock Preferred—Co. B		$50,000		
Eliminate holding company's 80%			$40,000	
Minority 20%				$10,000M
Capital Stock Common—Co. B		100,000		
Eliminate holding company's 90%			90,000	
Minority 10%				10,000M
Surplus—Co. B		18,000		
Applicable to Preferred—$6,000				
Eliminate holding company's 80%			4,800	
Minority 20%				1,200M
Applicable to Common—$12,000				
Eliminate holding company's 90%			10,800	
Minority 10%				1,200M
Surplus—Co. A	$15,600			15,600 S

Stock dividends.—If the holding company carries its investment at cost, stock dividends should be taken up by a debit to the investment account and a credit to surplus, as illustrated in the following example:

Company A purchased 90 per cent of the stock of Company B at January 1, 1920, paying $140,000 therefor. At that date Company B had a capital stock of $100,000 and a surplus of $50,000. During the year Company B made a profit of $25,000, and at the end of the year declared and issued a stock dividend of $40,000, of which Company A received $36,000. Assuming that Company A had no surplus at the beginning of the year and made no profits from its own operations, the working papers at the end of the year would be:

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B	$176,000			
Eliminate book value at acquisition:				
Capital stock: Original purchase.			$90,000	
Stock dividend			36,000	
Surplus: 90% of $50,000			45,000	
Goodwill				$5,000 G
Liabilities				
Capital Stock		$140,000		
Eliminate Co. A's 90%			$126,000	
Minority 10%				$14,000M
Surplus:				
Co. A	$36,000			36,000 S
Co. B		35,000		
Minority: 10% of $35,000 pres. surplus				3,500M
Elim. H. C.: 90% of 50,000 at acquis			45,000	
Surplus: 90% of 15,000 decrease				13,500*S

The surplus on the consolidated balance sheet will be $22,500, which is 90 per cent of the year's profits of Company B.

If the stock dividend were not taken up by the holding company, a portion of the capital stock of the subsidiary would have to be carried out to the balance sheet columns as surplus to appear in the consolidated balance sheet because the subsidiary earnings since the date of acquisition have been merged with the profits prior to acquisition and a portion of this surplus has been transferred to the capital stock account of the subsidiary.

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B	$140,000			
Eliminate book value at acquisition:				
Capital stock			$90,000	
Surplus: 90% of $50,000			45,000	
Goodwill				5,000 G
Liabilities				
Capital Stock—Co. B		$140,000		
Minority 10% of present stock				$14,000M
Elim. Co. A's 90% of stock at acquisition			$90,000	
Surplus				36,000 S
Surplus—Co. B		35,000		
Minority 10% of $35,000 present surplus				3,500M
Elim. Co. A's 90% of 50,000 surp. at acquisition			45,000	
Surplus: 90% of 15,000 decrease				13,500*S

If the holding company takes up its share of subsidiary profits and losses, no entry should be made on the holding company's books for the stock dividend, as it represents merely a transfer of a portion of the net worth from the subsidiary's surplus to its capital stock account. If Company A has taken up its $22,500 profits from Company B during the year, the working papers will appear as follows:

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B	$162,500			
Eliminate present book value:				
Capital stock: 90% of $140,000			$126,000	
Surplus: 90% of 35,000			31,500	
Goodwill				$5,000 G
Liabilities				
Capital Stock—Co. B		$140,000		
Eliminate Co. A's 90%			$126,000	
Minority 10%				$14,000M
Surplus:				
Co. A	$22,500			22,500 S
Co. B		35,000		
Eliminate Co. A's 90%			31,500	
Minority 10%				3,500M

Arbitrary entries in investment account.—In some instances a holding company will not take up the profits and losses of its subsidiary but will at intervals make entries of an arbitrary amount to raise or lower the investment account to an estimated present value. If the entry adjusts the investment to its present book value as measured by the capital stock and surplus accounts of the subsidiary, and if eliminations are made in the working papers on the basis of present book value, the effect will be to eliminate from the consolidated balance sheet any goodwill or negative goodwill in the stock purchase. To illustrate, Company A purchased 90 per cent of the stock of Company B, paying $115,000 therefor. At the date of acquisition Company B had a capital stock of $100,000 and a surplus of $20,000, so that its book value was $120,000. Ninety per cent was $108,000, and there was therefore a goodwill element of $7,000 in the purchase. The investment account was carried at cost until the end of the year at which time the subsidiary had a surplus of $50,000, making its book value $150,000, and 90 per cent thereof, $135,000. Company A thereupon made an entry debiting the investment account and

crediting surplus with $20,000 to raise the investment account from $115,000 to $135,000. If eliminations are made on the basis of present book values, the working papers will appear as follows:

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$135,000			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 50,000..			45,000	
Liabilities				
Capital Stock—Co. B.....		$100,000		
Eliminate holding company's 90%.			$90,000	
Minority interest 10%.				$10,000M
Surplus:				
Co. A.....	$20,000			20,000 S
Co. B.....		50,000		
Eliminate holding company's 90%			45,000	
Minority interest 10%				5,000M

These working papers show that the goodwill of $7,000 is eliminated, and that the holding company's surplus is only $20,000, whereas the holding company should have taken up its 90 per cent of the $30,000 profits for the year, or $27,000. Because of the erroneous results produced if such arbitrary entries are ignored, it is advisable to reverse them by adjusting entries in the consolidated working papers.

Chapter XII

MAJOR HOLDING COMPANY CONTROL THROUGH A MINOR HOLDING COMPANY

Outline of chapter.—This chapter will contain four sections devoted to the following subjects:

1. An explanation of the method by which a major holding company may control a group of corporations through the ownership of the stock of a minor holding company.
2. A discussion of the reasons why it is desirable for the holding companies, and particularly the minor holding company, to take up the subsidiary profits, losses and dividends through the investment accounts rather than to carry the investment accounts at cost.
3. An illustration of the preparation of consolidated working papers when the investment accounts have been charged with subsidiary profits and credited with subsidiary losses and dividends.
4. An illustration of the preparation of consolidated working papers when the investment accounts are carried at cost.

Major and minor holding company.—In the process of combining a group of corporations it frequently happens that one company will buy a controlling interest in the stock of another company which is itself a holding company owning stock in a subsidiary. The minor holding company controls only its own subsidiary, but the major holding company controls the minor holding company and thus controls the entire organization.

Advantage of taking up subsidiary profits, losses and dividends.—In discussing this subject we shall first consider the minor holding company and discuss the reasons why it is desirable for it to take up the profits, losses and dividends of its subsidiary; second, we shall consider the advantages resulting from having the major holding company also take up profits, losses and dividends.

If the minor holding company takes up the profits, losses and dividends of its subsidiary, the preparation of the con-

solidated balance sheet will be facilitated in three particulars: namely, the computation of the goodwill, the minority interest and the surplus.

The goodwill involved in the purchase of the minor holding company's stock by the major holding company is the excess of the purchase price over the book value of the minor holding company's stock at the date of acquisition. If the minor holding company has not taken up the profits of its subsidiary, its surplus will be under-stated because it will not include the profits which it has earned through the operations of its subsidiary. The under-statement of surplus means an under-statement of book value, and this in turn means an over-statement of goodwill. To illustrate, assume that Company B has a capital stock of $100,000 and a surplus of $50,000 arising from its own operations. It owns all of the stock of Company C but has not taken up the $25,000 profit earned by Company C since it acquired C's stock. Company A now purchases all of Company B's stock, paying $190,000 therefor. According to Company B's books which show a capital stock of $100,000 and a surplus of $50,000, the book value of B's stock appears to be $150,000, and the purchase of this stock by Company A at a price of $190,000 appears to involve a goodwill element of $40,000. But as a matter of fact Company B should have a surplus of $75,000 and a total book value of $175,000, so that the goodwill element is only $15,000.

In the second place, the computation of the minority interest will be facilitated if the minor holding company takes up the profits of its subsidiary. Returning to the illustration in the preceding paragraph, let us assume that Company A bought only 90 per cent of the stock of Company B. There is, therefore, a 10 per cent minority interest in Company B. These minority stockholders are entitled not only to 10 per cent of the profits from the minor holding company's own operations but also to 10 per cent of the profits accruing from the ownership of the subsidiary C stock. The minority interest in the surplus of Company B is therefore 10 per cent of $75,000, but it will be difficult to show this fact in the working papers if Company B's surplus appears at only $50,000.

In the third place, the computation of the surplus appearing on the consolidated balance sheet will be facilitated if the minor holding company has taken up the profit of its subsidiary. To illustrate, assume that Company A owns 90 per cent of the stock of Company B, and that Company B owns 80 per cent of the stock of Company C. The surplus on the consolidated balance sheet will include: (1) Company A's earnings from its own operations, (2) plus 90 per cent of the earnings of Company B since the date when Company A acquired its stock. These earnings of Company B should include 80 per cent of the earnings of Company C.

Now if Company B has taken up its earnings from Company C, the surplus on the consolidated balance sheet will be correctly stated by merely taking up 90 per cent of the total earnings of Company B since the date of acquisition. But if Company B has not taken up its earnings from Company C, a correct statement of the surplus of Company A will require taking up (1) 90 per cent of the profits from the operations of Company B since the date when A acquired the stock of B; and (2) 90 per cent of 80 per cent of the profits from the operations of Company C since the date when A acquired the stock of B.

Turning now to the advantages to be obtained if the major holding company also takes up the profits and losses of its subsidiary, it should be readily seen that the major holding company's surplus will in that case include all of the profits from its own operations and from the ownership of the stock of its subsidiaries. For in taking up 90 per cent of the earnings of Company B, which include B's share of the profits of C, the major holding company has automatically taken up the proper proportion of the profits of Company C. The surplus on the consolidated balance sheet will therefore be the surplus of the major holding company only, and it will not be necessary to make involved adjustments on the working papers to take up the proper proportions of the profits of the minor holding company and its subsidiary.

First illustration: All inter-company profits taken up.—If all subsidiary profits have been taken up by the major and minor holding companies, the preparation of the consolidated working papers is a very simple matter, for all eliminations are based on the present book values of the stock holdings. As an illustration assume the following facts:

1. Company A owns 90 per cent of the stock of Company B
2. Company A owns 20 per cent of the stock of Company C
3. Company B owns 60 per cent of the stock of Company C
4. Company C owns 85 per cent of the stock of Company D

Company A is therefore the major holding company, for it controls the entire organization. Company B is a minor holding company, for it owns a majority of the stock of Company C. Company C is also a minor holding company, for it owns a majority of the stock of Company D.

All companies have taken up the profits, losses and dividends of their subsidiaries; consequently the investment accounts represent the present book value of the stock holdings plus any goodwill or minus any negative goodwill involved in the stock purchases. Therefore eliminations will be based on present book values. Following are the balance sheets at December 31, 1920.

Assets	*Co. A*	*Co. B*	*Co. C*	*Co. D*
Investment in Stock of Co. B (90%)	$92,493			
Investment in Stock of Co. C (20%)	14,090			
Investment in Stock of Co. C (60%)		$ 41,070		
Investment in Stock of Co. D (85%)			$34,175	
Cash	37,850	60,100	31,275	$38,500
	$144,433	$101,170	$65,450	$38,500
Liabilities				
Capital Stock	$100,000	$75,000	$50,000	$30,000
Surplus	44,433	26,170	15,450	8,500
	$144,433	$101,170	$65,450	$38,500

The following consolidated balance sheet is prepared from the working papers on pages 93 and 94.

COMPANY A AND SUBSIDIARIES B, C AND D

CONSOLIDATED BALANCE SHEET

December 31, 1920

Assets		
Goodwill		$ 5,690
Cash		167,725
		$173,415
Liabilities		
Minority Interests:		
Company B (10%)	$10,117	
Company C (20%)	13,090	
Company D (15%)	5,775	$28,982
Capital:		
Capital Stock	100,000	
Surplus	44,433	144,433
		$173,415

COMPANY A AND SUBSIDIARIES B, C AND D

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

December 31, 1920

Assets	*Co. A*	*Co. B*	*Co. C*	*Co. D*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$92,493					
Eliminate present book value:						
Capital stock: 90% of $75,000					$67,500	
Surplus: 90% of 26,170					23,553	
Goodwill						$1,440 G
Investment in Stock of Co. C (20%)	14,090					
Eliminate present book value:						
Capital stock: 20% of $50,000					10,000	
Surplus: 20% of 15,450					3,090	
Goodwill						1,000 G
Investment in Stock of Co. C (60%)		$41,070				
Eliminate present book value:						
Capital stock: 60% of $50,000					30,000	
Surplus: 60% of 15,450					9,270	
Goodwill						1,800 G
Investment in Stock of Co. D (85%)			$34,175			
Eliminate present book value:						
Capital stock: 85% of $30,000					25,500	
Surplus: 85% of 8,500					7,225	
Goodwill						1,450 G
Cash	37,850	60,100	31,275	$38,500		167,725
	$144,433	$101,170	$65,450	$38,500	$176,138	$173,415

Liabilities	*Co. A*	*Co. B*	*Co. C*	*Co. D*	*Elim.*	*C. B. S.*
Capital Stock:						
Company A	$100,000					$100,000
Company B		$75,000				
Eliminate Co. A's 90%					$67,500	
Minority 10%						7,500 M in Co. B
Company C			$50,000			
Eliminate Co. A's 20%					10,000	
Eliminate Co. B's 60%					30,000	
Minority 20%						10,000 M in Co. C
Company D				$30,000		
Eliminate Co. C's 85%					25,500	
Minority 15%						4,500 M in Co. D
Surplus:						
Company A	44,433					44,433 S
Company B		26,170				
Eliminate Co. A's 90%					23,553	
Minority 10%						2,617 M in Co. B
Company C			15,450			
Eliminate Co. A's 20%					3,090	
Eliminate Co. B's 60%					9,270	
Minority 20%						3,090 M in Co. C
Company D				8,500		
Eliminate Co. C's 85%					7,225	
Minority 15%						1,275 M in Co. D
	$144,433	$101,170	$65,450	$38,500	$176,138	$173,415

This illustration shows that when all of the holding companies have taken up their proportions of subsidiary profits, losses and dividends, the preparation of the working papers is not in any way complicated by the fact that the major holding company holds its control of the organization by ownership through a minor holding company.

The goodwill is the excess of the various investment accounts over the present book value of the stock holdings.

The minority interests are their proportions of the capital stock and surplus accounts of the companies in which they own stock.

The surplus appearing on the consolidated balance sheet is the major holding company's surplus only, for it includes the subsidiary profits taken up.

Second illustration: Inter-company profits not taken up.—To illustrate the simplest method of preparing consolidated balance sheet working papers when the major and minor holding companies have carried their investment accounts at cost, the same group of companies will be used as in the first illustration. It will now be assumed, however, that no subsidiary profits have been taken up; the investment accounts are all carried at cost; and dividends received from subsidiaries have been credited to surplus. All essential facts will be restated so that reference to the preceding illustration will not be necessary.

The various stock purchases were made at dates and prices as follows:

1. At January 1, 1918, Company A purchased 80 per cent of the stock of Company B, paying $85,000.
2. At January 1, 1919, Company B purchased 60 per cent of the stock of Company C, paying $45,000.
3. At January 1, 1920, Company A purchased 10 per cent of the stock of Company B, paying $10,000.
4. At January 1, 1920, Company A purchased 20 per cent of the stock of Company C, paying $14,000.
5. At January 1, 1920, Company C purchased 85 per cent of the stock of Company D, paying $38,000.

Following are the balance sheets of the four companies at December 31, 1920. These are the same balance sheets as before, except that the investment accounts are carried at cost, and the surplus accounts are different because the holding companies have taken up subsidiary dividends as profits instead

of crediting surplus with subsidiary profits and charging it with subsidiary losses.

Assets	*Co. A*	*Co. B*	*Co. C*	*Co. D*
Investment in Stock of Co. B (90%) Cost	$95,000			
Investment in Stock of Co. C (20%) Cost	14,000			
Investment in Stock of Co. C (60%) Cost		$45,000		
Investment in Stock of Co. D(85%) Cost			$38,000	
Cash	37,850	60,100	31,275	$38,500
	$146,850	$105,100	$69,275	$38,500
Liabilties				
Capital Stock	$100,000	$75,000	$50,000	$30,000
Surplus	46,850	30,100	19,275	8,500
	$146,850	$105,100	$69,275	$38,500

The fact that the investment accounts are carried at cost makes the preparation of the consolidated working papers far more difficult than in the preceding illustration. In the first place, Companies B, C and D all have minority interests; these minority stockholders are entitled to their proportions of the true surplus of the respective companies. But in the case of Companies B and C, the surplus accounts do not represent the true surplus because these minor holding companies have credited surplus with dividends received from their subsidiaries rather than with the profits earned by the subsidiaries since the dates of acquisition. If the dividends have exceeded the profits earned during the period of ownership, the surplus accounts are over-stated; if the profits earned by the subsidiaries have exceeded the dividends paid by them, the surplus accounts of the holding companies are under-stated.

In the second place, the consolidated balance sheet must show the true surplus of Company A, but the surplus account in Company A's balance sheet does not represent the true surplus of Company A for the same reason that the surplus accounts of Companies B and C do not represent their true surplus; Company A has taken up dividends instead of taking up the profits and losses of its subsidiaries.

The first step in the preparation of consolidated working papers will therefore be the ascertaining of the true surplus accounts of the several companies. This will be accomplished by building up a statement showing what the several surplus accounts would be if each company had taken up subsidiary

profits and losses instead of subsidiary dividends. Having ascertained these true surplus balances, adjustments will be made on the working papers to raise or lower the surplus accounts to the true balances. That is, if subsidiary profits have exceeded dividends, surplus will be credited; the offsetting debit will be made against the investment accounts to adjust them to the balances which they would have if the holding companies had followed the correct accounting procedure. On the other hand, if subsidiary dividends have exceeded subsidiary profits, the holding companies' surplus accounts will be debited for the excess of the dividends over the profits; and the offsetting credits will be made in the investment accounts to reduce them; this reduction is necessitated by the fact that dividends in excess of profits reduce the value of the subsidiary net assets and hence reduce the value of the investments.

Having made the adjustments indicated above, the investment accounts and surplus accounts will have been adjusted to the same basis as in the preceding illustration, and eliminations can be made on the basis of present book values, as in the preceding illustration.

The following statement shows the operating profits and losses of the four companies from January 1, 1918, to December 31, 1920, as well as the credits to surplus for subsidiary dividends taken up, and the debits to surplus for dividends paid. The final balances agree with the surplus balances shown in the balance sheet on page 96.

STATEMENT OF SURPLUS ACCOUNTS PER BOOKS

(Subsidiary Profits and Losses Not Taken Up, but Subsidiary Dividends Received Treated as Income)

	Co. A	*Co. B*	*Co. C*	*Co. D*
Surplus, January 1, 1918	$25,000	$30,000	$20,000	$5,000
Profits of 1918:				
From operations	10,000	3,000*	5,000	6,000
Dividends received	3,600			
Total	$38,600	$27,000	$25,000	$11,000
Less Dividends paid	6,000	4,500	3,000	1,500
Surplus, December 31, 1918	$32,600	$22,500	$22,000	$9,500
Profits of 1919:				
From operations	8,000	5,000	4,000*	5,000
Dividends received	3,600	1,800		
Total	$44,200	$29,300	$18,000	$14,500
Less Dividends paid	6,000	4,500	3,000	1,500
Surplus, December 31, 1919	$38,200	$24,800	$15,000	$13,000
Profits of 1920:				
From operations	10,000	8,000	6,000	3,000*
Dividends received:				
From Co. B	4,050			
From Co. C	600	1,800		
From Co. D			1,275	
Total	$52,850	$34,600	$22,275	$10,000
Less Dividends paid	6,000	4,500	3,000	1,500
Surplus, December 31, 1920	$46,850	$30,100	$19,275	$8,500

The following Statement of Adjusted Surplus and Investment Accounts shows the method of arriving at the necessary adjustments. This statement is built up from the foregoing statement of surplus accounts, and shows the entries in surplus and investment accounts which should have been made by the several companies to record profits, losses and dividends in the proper manner. At the end of the statement there are shown the surplus and investment account balances which result from a proper accounting method; by comparing these balances with the balances per the companies' books the necessary adjustments are ascertained.

COMPANY A AND SUBSIDIARIES B, C AND D

STATEMENT OF ADJUSTED SURPLUS AND INVESTMENT ACCOUNTS

	Company A		Company B		Company C	Company D
	Investment in B	*Investment in C*	*Surplus*	*Investment in C*	*Surplus*	*Investment in D*	*Surplus*
YEAR 1918:							
Cost of A's investment in B (80%)	$85,000						
Surplus, January 1, 1918			$25,000		$30,000		$20,000	$5,000
Profits of 1918:							
From own operations			10,000		3,000*		5,000	6,000
From subsidiaries:							
A's 80% of B's $3,000 loss	2,400*		2,400*					
Total			32,600		27,000		25,000	11,000
Less Dividends Paid			6,000		4,500		3,000	1,500
Surplus, December 31, 1918			26,600		22,500		22,000	9,500
Investment account entries for dividends received:								
A's 80% of B's $4,500 dividend	3,600*							
YEAR 1919:								
Cost of B's investment in C (60%)				45,000				
Profits of 1919:								
From own operations			8,000		5,000		4,000*	5,000
From subsidiaries:								
B's 60% of C's $4,000 loss				2,400*	2,400*			
A's 80% of B's $2,600 gain ($5,000—$2,400)	2,080		2,080					
Total			36,680		25,100		18,000	14,500
Less Dividends Paid			6,000		4,500		3,000	1,500
Surplus, December 31, 1919			30,680		20,600		15,000	13,000
Investment account entries for dividends received:								
A's 80% of B's $4,500 dividend		3,600*						
B's 60% of C's 3,000 dividend				1,800*				

STATEMENT OF ADJUSTED SURPLUS AND INVESTMENT ACCOUNTS — *Continued*

YEAR 1920:								
Cost of A's investment in B (10%)	10,000							
Cost of A's investment in C (20%)		$14,000						
Cost of C's investment in D (85%)						$38,000		
Profits of 1920:								
From own operations			10,000		8,000		6,000	3,000*
From subsidiaries:								
C's 85% of D's 3,000 loss						2,550*	2,550*	
B's 60% of C's $3,450 profit ($6,000—$2,550)				2,070	2,070			
A's 20% of C's $3,450 profit		690	690					
A's 90% of B's $10,070 profit ($8,000+$2,070)	9,063		9,063					
Total			50,433		30,670		18,450	10,000
Less Dividends Paid			6,000		4,500		3,000	1,500
Adjusted Surplus—December 31, 1920			44,433		26,170		15,450	8,500
Investment account entries for dividends received:								
A's 90% of B's $4,500 dividend	4,050*							
A's 20% of C's 3,000 dividend		600*						
B's 60% of C's 3,000 dividend				1,800*				
C's 85% of D's 1,500 dividend						1,275*		
Adjusted balances of investment accounts	92,493	14,090		41,070		34,175		
Investment and surplus accounts per books	95,000	14,000	46,850	45,000	30,100	38,000	19,275	8,500
Adjustments	$2,507Cr.	$90Dr.	$2,417Dr.	$3,930Cr.	$3,930Dr.	$3,825Cr.	$3,825Dr.	0

*Deductions.

In the following working papers, the adjustments are made in the respective investment and surplus accounts. Eliminations are then made on the basis of present book values, exactly as was done in the first illustration. A consolidated balance sheet is not set up from these working papers, as it would be identical with the one in the first illustration.

COMPANY A AND SUBSIDIARIES B, C AND D

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

December 31, 1920

Assets	*Co. A*	*Co. B*	*Co. C*	*Co. D*	*Adjustments* Dr.	*Adjustments* Cr.	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$95,000							
Adjustment for Co. B dividends received in excess of profits earned						$2,507(A)		
Eliminate present book value:								
Capital stock: 90% of $75,000							$67,500	
Surplus: 90% of 26,170							23,553	
Goodwill								$1,440 G
Investment in Stock of Co. C (20%) Cost	14,000							
Adjustment for Co. C profits in excess of dividends received					90(A)			
Eliminate present book value:								
Capital stock: 20% of $50,000							10,000	
Surplus: 20% of 15,450							3,090	
Goodwill								1,000 G
Investment in Stock of Co. C (60%) Cost		$45,000						
Adjustment for Co. C dividends received in excess of profits earned						3,930(B)		
Eliminate present book value:								
Capital stock: 60% of $50,000							30,000	
Surplus: 60% of 15,450							9,270	
Goodwill								1,800 G
Investment in Stock of Co. D (85%) Cost			$38,000					
Adjustment for Co. C dividends received in excess of profits earned						3,825(C)		
Eliminate present book value:								
Capital stock: 85% of $30,000							25,500	
Surplus: 85% of 8,500							7,225	
Goodwill								1,450 G
Cash	37,850	60,100	31,275	$38,500				167,725
	$146,850	$105,100	$69,275	$38,500	$90	$10,262	$176,138	$173,415

CONSOLIDATED BALANCE SHEET—WORKING PAPERS—*Continued*

Liabilities	*Co. A*	*Co. B*	*Co. C*	*Co. D*	*Adjustments* Dr.	*Adjustments* Cr.	*Elim.*	*C. B. S.*	
Adjustment column totals forward					$90	$10,262			
Capital Stock:									
Company A	$100,000							$100,000	
Company B		$75,000							
Eliminate Co. A's 90%							$67,500		
Minority 10%								7,500	M in B
Company C			$50,000						
Eliminate Co. A's 20%							10,000		
Eliminate Co. B's 60%							30,000		
Minority 20%								10,000	M in C
Company D				$30,000					
Eliminate Co. C's 85%							25,500		
Minority 15%								4,500	M in D
Surplus:									
Company A	46,850								
Adjustment for excess of subsidiary dividends taken up over profits earned					2,417(A)				
Adjusted surplus								44,433	S
Company B		30,100							
Adjustment for excess of subsidiary dividends taken up over profits earned					3,930(B)				
Adjusted surplus = $26,170									
Eliminate Co. A's 90% of $26,170							23,553		
Minority 10% of 26,170								2,617	M in B
Company C			19,275						
Adjustment for excess of subsidiary dividends taken up over profits earned					3,825(C)				
Adjusted surplus = $15,450									
Eliminate Co. A's 20% of $15,450							3,090		
Eliminate Co. B's 60% of 15,450							9,270		
Minority 20% of 15,450								3,090	M in C
Company D				8,500					
Eliminate Co. C's 85% of $8,500							7,225		
Minority 15% of 8,500								1,275	M in D
	$146,850	$105,100	$69,275	$38,500	$10,262	$10,262	$176,138	$173,415	

CHAPTER XIII

UNREALIZED INTER-COMPANY PROFITS

Profits in inventories.—When one constituent company sells goods at a profit to another constituent company, the minority stockholders of the selling company have a right to consider that the profit has been realized since the goods have been sold to a company in which they have no interest. The holding company which controls the organization and which looks upon the various subsidiaries virtually as departments of the organization, should not consider the profit as realized until the goods have been resold to a purchaser outside of the organization.

Therefore, if, at the date of the consolidated balance sheet, the inventories of any of the related companies contain goods which have been purchased from another related company after the combination was effected, the inventories should be analyzed to determine how much of their present cost or carrying value is composed of profits added by the selling companies. After this unrealized profit has been ascertained a reserve should be created out of the holding company's surplus for the holding company's portion of such unrealized profit.

To illustrate, it will be assumed that Company A owns 90 per cent of the stock of Company B. Company B has sold goods to Company A during the year at a profit, and the inventory of Company A at the end of the year includes goods purchased from Company B on which the latter company made a profit of $1,000. Since Company A, in taking up its share of the profits of Company B, has taken up $900 of this profit, a reserve should be created by deducting $900 from the holding company's surplus and transferring it to a reserve.

Position of reserve on the balance sheet.—There are two possible methods of showing the reserve for unrealized profits on the consolidated balance sheet. The first is as a deduction from inventories, and the second is on the liability side under the caption of reserves. The former method is usually em-

ployed and is theoretically correct, for inventories should be priced at cost (unless market is lower) and cost should not include the organization's share of unrealized profits resulting from transfers from one related company to another.

Conflicting opinions as to amount of reserve.— Some accountants set up a reserve for the entire amount of the unrealized profit instead of for the holding company's proportion thereof. This is permissible for tax purposes, for the tax law views the related companies as a unit without consideration of minority interests. But the commercial purpose of a consolidated balance sheet is to show the interests of the holding company's stockholders and the minority stockholders in the total assets of the consolidation. From the commercial viewpoint, the minority stockholders are outsiders and their share of the profit is earned as soon as the goods are sold to another corporation in which they have no interest.

Complications in computation of reserve.—When the organization is composed of a number of companies, the computation of the reserve for unrealized profits in inventories may be complicated by the fact that:

1. The profits are made by a subsidiary of a minor holding company;
2. The profits are cumulative.

The essential principle to bear in mind is that, so far as the minority interest of the company making the profit by sale or service is concerned, the profit is earned, but the holding company taking up the profit should set up a reserve for its pro-rata share of the portion which has not been realized by sales outside the organization.

Profits of subsidiary of minor holding company.—Three illustrations will be given to show the method of determining the amount of the reserve.

First illustration: A owns all of B; B owns 90 per cent of C. B's inventory contains unrealized profits of $1,000 on goods purchased from C. Since B has taken up 90 per cent of the unrealized profit, and A has taken up the same amount by taking up all of B's profit, a reserve of 90 per cent of $1,000, or $900, should be set up.

Second illustration: A owns 80 per cent of B; B owns 90 per cent of C. A's inventory contains unrealized profits of $1,000 on goods purchased from C. Since B has taken up 90 per cent of the unrealized profit made by C, and A has taken up 80 per cent of B's 90 per cent in taking up its share of B's profit, the reserve should be 80 per cent of 90 per cent of $1,000, or $720.

Third illustration: A owns 80 per cent of B and 10 per cent of C; B owns 90 per cent of C. A's inventory contains unrealized profits of $1,000 on goods purchased from C. B has taken up 90 per cent of the unrealized profit, and A has taken up 80 per cent of this 90 per cent in taking up its share of B's profit. A has also taken up 10 per cent of the unrealized profit by taking up its share of C's profit. Since A has taken up 72 per cent plus 10 per cent of the unrealized profit, it should set up a reserve for 82 per cent or $820. The remaining $180 is properly included in the minority interest of Company B; these stockholders own 20 per cent of Company B which has taken up 90 per cent of the profit, and this profit is realized to the minority of Company B since they are outsiders so far as concerns the organization controlled by Company A.

Cumulative profits.—As an illustration of cumulative unrealized profits in inventories, it will be assumed that Company A owns 90 per cent of the stock of Company B, while Company B owns 80 per cent of the stock of Company C. The inventory of Company A contains goods which were put through one process by Company C and sold to Company B at a profit of $800; Company B put them through another process and sold them to Company A at a profit of $1,200. The reserve is computed as follows:

Company C's profits:	
90% of 80% of $800	$ 576
Company B's profits:	
90% of $1,200	1,080
Total reserve	$1,656

Profits from sales before combination.—If the inventories contain goods which were sold by one company to another before the holding company acquired control of the selling company, no reserve should be created because the holding company did not take up a share of such profits and should not be required to reduce its surplus by an amount which has not been included therein. The companies were not related when

the sale took place, and hence the profit is not inter-company profit.

Inter-company profits in construction.—When one related company produces fixed assets for another company and makes a profit on the construction, a reserve should be created to eliminate the holding company's proportion of such profit and reduce the fixed assets to cost. As already shown in connection with inventories, the cost may properly include the profit made by the minority stockholders of the selling company. The holding company can not equitably ask the minority stockholders of its subsidiary to forego their share of the profit on work done for a company in which they have no interest.

To illustrate, assume that Company A owns 90 per cent of the stock of Company B. After the combination is effected, the latter company sells fixed assets to Company A at a profit of $1,000. At the end of the year, Company A will take up $900 of the profit which Company B made on the sale, and it should therefore create a reserve of $900 for unrealized profit in fixed assets.

The question of inter-company profits on construction of fixed assets is a much more complex one than that of inter-company profits in inventories. Inter-company profits in inventories will become realized profits when the goods are sold to outsiders and the reserve will disappear when the goods are disposed of. In the case of fixed assets, however, the property is not ordinarily disposed of through sale, and it might seem therefore that the reserve should be kept intact and appear as a deduction on the balance sheet at the original amount so long as the fixed assets are owned. But it should be remembered that the fixed assets are virtually disposed of gradually through use and depreciation, and it would therefore seem logical to reduce the depreciation charges to a basis of inter-company cost. This view is strengthened when it is remembered that depreciation should be based on cost, and that cost cannot be two different things for two different purposes. If cost for balance sheet purposes is purchase price less inter-company profit, then cost for depreciation purposes should be the same amount. If manufacturing expense is charged with depreciation on the purchase price, the costs of manufacture will be over-stated since depreciation will have been computed on a value in excess of the cost to the organization.

It is not difficult to put this theory into practice if the holding company owns the asset on which the inter-company profit was made. Two methods are available:

1. The holding company may write down the asset to inter-company cost by debiting surplus and crediting the asset account instead of crediting a reserve for inter-company profit. Depreciation will then be computed on the carrying value of the property as shown by the asset account.

2. The holding company may carry the reserve and compute depreciation on the carrying value of the property as measured by the debit balance in the asset account minus the credit balance in the reserve for inter-company profit.

To illustrate, assume that Company A owns 90 per cent of the stock of Company B, and that during the year Company B manufactured for Company A machinery which it delivered to them at the end of the year, billing them at $25,000. The profit made by Company B was $5,000. Company A took up 90 per cent of this amount, or $4,500, in taking up its share of the profits of Company B. If Company A follows the first method suggested above, it will debit its surplus and credit the machinery account $4,500, thus reducing the asset to $20,500 which is inter-company cost after allowing the minority stockholders of Company B their 10 per cent of the profit. Depreciation will then be computed on $20,500. If Company A follows the second method suggested above, it will debit surplus and credit a reserve for unrealized profit in fixed assets $4,500; it will then compute depreciation on the $25,000 balance of the asset account minus the $4,500 balance of the reserve for inter-company profit.

The theory is not so easily put into practice if the company making the profit sold the assets to another affiliated company instead of to the holding company. To illustrate, assume that Company A owns 90 per cent of the stock of Company B and 80 per cent of the stock of Company C. Company C has sold machinery to Company B for $50,000 which cost $40,000. When Company A takes up its 80 per cent of the profits of Company C, it takes up $8,000 of this unrealized inter-company profit and should therefore create a reserve of $8,000. The first method suggested above is not practicable in this case; the asset is on Company B's books while the unrealized profit must be taken out of Company A's surplus. It is impossible to write down the asset on Company B's books, because that would involve a debit to Company B's surplus which would be

improper, because the inter-company profit went into A's surplus and not into B's. The asset will therefore go on B's books at $50,000, and the reserve will be set up at $8,000 on A's books.

For consolidated balance sheet purposes the cost of the asset was $42,000, but Company B will compute depreciation on a basis of $50,000, which was the cost to Company B as a separate corporation. If the rate of depreciation is 10 per cent, the depreciation on a straight line basis will be $5,000 annually. But from the standpoint of the organization as a unit Company B has over-stated its manufacturing costs by 10 per cent of $8,000 or $800, and if all of the goods manufactured by Company B during the year have been sold outside the organization the profits of the organization have been under-stated $800. In other words, according to the theory which makes depreciation a manufacturing expense, 10 per cent of the machinery has now been converted into finished goods and sold. Ten per cent of the unrealized profit on fixed assets is thereby realized by converting the fixed assets into finished goods and selling them. The holding company A would therefore be justified, in the author's opinion, in transferring 10 per cent of the $8,000 reserve or $800 to its surplus account, thus reducing the reserve on the holding company's books to $7,200. The asset would then appear on the consolidated balance sheet as follows:

Machinery		$50,000
Less Reserve for inter-company profit on construction	$7,200	
Reserve for depreciation	5,000	12,200
		$37,800

This treatment seems theoretically correct since it produces the same result which would be produced by either the first or second method if the holding company had itself purchased the asset from Company C. In that case Company A would carry the asset on its own books at $42,000. The depreciation at 10 per cent would be $4,200, and the carrying value at the end of the first year would be:

Machinery (at cost less inter-company profit)	$42,000
Less Depreciation	4,200
	$37,800

There is a still further complication if the finished goods have not been sold or have been sold to another company within the organization. In that case the inter-company profit on construction has merely been converted into inter-company profit in inventories, and, as this inter-company profit has not been realized by sales outside the organization, it should appear in the reserve for inter-company profits in inventories on the consolidated balance sheet.

Illustration of working papers.—The method of obtaining the reserves for the consolidated balance sheet will depend upon whether or not they have been set up on the books of the holding company. If they have been set up, they will appear in the balance sheet of the holding company and will be merely carried out to the consolidated balance sheet columns. If they have not been set up on the holding company's books, they will be deducted from the holding company's surplus on the working papers, as indicated below:

CONSOLIDATED BALANCE SHEET WORKING PAPERS

	Co. A	*Co. B*	*Elim.*	*C. B. S.*
Surplus—Co. A	$40,000			
Reserve for int.-co. profit in inventories				$ 900 R
Reserve for int.-co. profit in construction				4,500 R
Surplus				34,600 S

Chapter XIV

CONSOLIDATED PROFIT AND LOSS AND SURPLUS STATEMENTS

SEPARATE WORKING PAPERS

Working papers based on statements or trial balances.—At the close of each accounting period it is customary to prepare a consolidated profit and loss statement, a consolidated surplus statement and a consolidated balance sheet. There are two methods available for making the working papers for these statements.

First, they may be prepared from the statements of the holding company and its subsidiaries after their books are closed. If this method is adopted there will be a separate set of working papers for the revenue statement, the surplus statement and the balance sheet.

Second, they may be prepared from the trial balances of the holding company and its subsidiaries before the books are closed. If this method is adopted there will be a single set of working papers from which all of the consolidated statements will be prepared.

The first method will be illustrated in this chapter; the second method will be illustrated in Chapter XV.

Consolidated revenue statement—Working papers.—When the consolidated revenue statement is prepared from the revenue statements of the holding company and the subsidiaries, the statement may be divided into a cost of goods sold statement and a profit and loss statement, or both sections may be combined in a single statement. In either event, the working papers should contain columns for each company, two columns for adjustments if necessary, a column for inter-company eliminations, and one for the consolidated figures. The procedure may be summarized as follows:

1. Combine all similar items of income and expense.
2. Eliminate all inter-company nominal accounts.
   All inter-company transactions should have been taken

   up on the books of both companies which were parties to the transaction. If they have not been taken up, adjustments will be required in the working papers.
3. Make adjustments for inter-company profits as follows:
   a. Profits in inventories at the beginning of the period.—(1) If the beginning of the period was also the date of acquisition, make no adjustment as the profits were not inter-company profits. (2) If the beginning of the period was subsequent to the date of acquisition, make adjustment by reducing the inventories; this adjustment is equivalent to a credit to cost of sales (since the opening inventories are debited to cost of sales) and a debit to the holding company's surplus as of the beginning of the period. Only the credit will be shown in the revenue statement working papers; the debit will appear in the surplus statement working papers.
   b. Profits in inventories at the end of the period.—Make adjustment by reducing the inventories; this adjustment is equivalent to a debit to cost of sales since the closing inventories are credited to cost of sales, and a credit to reserve for inter-company profit in inventories. Only the debit will be shown in the revenue statement working papers.
   c. Profit on construction during the period.—Adjust by a reduction of the nominal account showing the profit; this adjustment is equivalent to a debit to the income account and a credit to the reserve.
4. From the total consolidated net profit:
   Deduct the minority interests in the profits of the subsidiaries, to obtain the net increase or decrease in the profits of the holding company.

Consolidated surplus statement—Working papers.—When the consolidated surplus statement is prepared from the surplus statements of the holding company and the subsidiaries, the working papers should contain columns for each company, two columns for adjustments if necessary, a column for inter-company eliminations, a column for the minority interest in the surplus accounts of the subsidiaries, and a column for the consolidated surplus figures. The procedure may be summarized as follows:

1. Enter the holding company's surplus as of the beginning of the period; make adjustment for any inter-company

profits in inventories at the beginning of the period which were not provided for on the books of the holding company. Carry the adjusted surplus to the consolidated surplus column.

2. Enter the surplus of each subsidiary as of the beginning of the period.
   a. Carry the minority interests thereof to the minority column.
   b. If the holding company has followed the procedure of taking up its share of subsidiary profits and losses, eliminate the holding company's percentage of the subsidiary's surplus at the beginning of the period.
   c. If the holding company has carried the investment account at cost, eliminate the holding company's percentage of the surplus at the date of acquisition, and carry to the consolidated surplus column the holding company's percentage of the increase or decrease in subsidiary surplus since the date of acquisition.
3. Foot the consolidated surplus column; the total should be the consolidated surplus of the organization at the beginning of the period, and should tie up with the surplus appearing on the consolidated balance sheet prepared at that date.
4. Enter the earnings of each company, the earnings of the minority and the consolidated earnings for the year, as shown by the consolidated profit and loss statement working papers.
5. Enter the dividends of each company, eliminate intercompany dividends, deduct dividends paid to minority holders in the minority column, and deduct dividends paid by the holding company in the consolidated column.

The balance of the minority column should be the minority's interest in the surplus of the subsidiaries, and the balance of the consolidated column should be the consolidated surplus at the end of the period and should tie up with the surplus shown in the consolidated balance sheet.

Outline of illustrations of separate working papers.—The procedure of preparing working papers depends as indicated in paragraph 2 of the preceding section, upon whether the holding company carries its investment account at cost or takes up its share of subsidiary profits and losses. It also depends upon whether the subsidiaries have paid any dividends during

the period. The following illustrations will indicate the procedure under various combinations of these conditions.

Group I. Subsidiary profits and losses up to beginning of period taken up by holding company:

First illustration: No dividends paid by subsidiaries.
Second illustration: Dividends paid by subsidiaries taken up by holding company as credit to Investment account.

Group II. Investment carried at cost:

Third illustration: No dividends paid by subsidiaries.
Fourth illustration: Dividends paid by subsidiaries taken up by the holding company as a credit to Profit and Loss.

First illustration: Consolidated profit and loss statement.—At December 31, 1921, Company A owns 90 per cent of the stock of Company B, which it purchased five years prior, and 80 per cent of the stock of Company C, which it purchased at January 1, 1921. Following are the revenue statements of the three companies for the year 1921:

COMPANY A AND SUBSIDIARIES B AND C

PROFIT AND LOSS STATEMENTS (*Exhibit A*)

For the Year Ending December 31, 1921

	Co. A	*Co. B*	*Co. C*
Gross Sales	$300,000	$225,000	$120,000
Less Returned Sales and Allowances	3,000	2,000	1,000
Net Sales	297,000	223,000	119,000
Less Cost of Goods Sold (Exhibit B)	215,000	175,000	80,000
Gross Profit on Sales	82,000	48,000	39,000
Less Selling Expenses	23,000	22,000	15,000
Net Profit on Sales	59,000	26,000	24,000
Less General and Administrative Expenses	22,000	11,000	3,000
Net Profit on Operations	37,000	15,000	21,000
Add Miscellaneous Income:			
Rent of Equipment to Company B	3,000		
Bond Interest Received from Company C		2,000	
Total	40,000	17,000	21,000
Less Bond Interest Paid	6,000		2,500
Net Profit for the Year	$34,000	$17,000	$18,500

COMPANY A AND SUBSIDIARIES B AND C

(Exhibit B)

STATEMENT OF COST OF GOODS SOLD

For the Year Ending December 31, 1921

	Company A		Company B		Company C	
Inventory, Goods in Process, January 1, 1921	$25,000		$30,000			
Materials Used:						
Inventory, January 1, 1921	$40,000		$15,000		$15,000	
Purchases	145,000		95,000		76,000	
Total	185,000		110,000		91,000	
Less Inventory, December 31, 1921	50,000		25,000		11,000	
Materials Used	135,000		85,000		80,000	
Direct Labor	85,000		65,000			
Manufacturing Expense	70,000	290,000	40,000	190,000		
Total		315,000		220,000		
Less Goods in Process, December 31, 1921		55,000		25,000		
Cost of Goods Manufactured		260,000		195,000		
Add Inventory of Finished Goods, January 1, 1921				30,000		
Total		260,000		225,000		
Less Inventory of Finished Goods, December 31, 1921		45,000		50,000		
Cost of Goods Sold		$215,000		$175,000		$80,000

Company C does no manufacturing, but deals only in raw materials, selling to outsiders and to Companies A and B. Both Company B and Company A manufacture; Company B sells to Company A and to outsiders; Company A sells to outsiders only.

Company A has taken up its share of the profits of Company B in prior years, but has taken up no subsidiary profits for 1921. Therefore Company A's profit and loss statement contains no figures for subsidiary profits or dividends.

The inventories at January 1, 1921, contained inter-company profits made by sales between companies as follows:

	Profit Made by Co. B	*Profit Made by Co. C*
Company A's Inventories:		
Raw Materials	$2,000	$1,000
Goods in Process	1,500	800
Company B's Inventories:		
Raw Material		500
Goods in Process		800
Finished Goods		250

The inventories at December 31, 1921, contained profits made by sales between companies as follows:

	Profit Made by Co. B	*Profit Made by Co. C*
Company A's Inventories:		
Raw Materials	$2,500	$1,200
Goods in Process	800	200
Finished Goods	1,800	1,500
Company B's Inventories:		
Raw Materials		500
Goods in Process		1,000
Finished Goods		1,300

Company C sold $60,000 worth of goods to Company B during the year and $35,000 worth to Company A. Company B sold $75,000 worth to Company A. Following are the working papers and the consolidated statements.

The first step is to ascertain the adjustments to be made in the working papers for inter-company profits in inventories. Since Company C was not a part of the organization prior to January 1, 1921, the profits which it made on sales to Company A and Company B prior to that date were not inter-company profits, and hence are ignored. The profit made by Company B on the goods in Company A's inventories at January 1, 1921,

must be considered. Company A's inventory at January 1 contained goods on which Company B had made a profit of $3,500. Since Company A owns 90 per cent of the stock of Company B the reserve at January 1, 1921, will be $3,150. Of this total, $1,800 will be deducted from the inventory of raw materials, and $1,350 from the inventory of goods in process.

The reserves for inventories at December 31, 1921, are computed as follows:

Company A:		
Raw Materials:		
90% of $2,500 profit made by Co. B	$2,250	
80% of 1,200 profit made by Co. C	960	$3,210
Goods in Process:		
90% of $800 profit made by Co. B	720	
80% of 200 profit made by Co. C	160	880
Finished Goods:		
90% of $1,800 profit made by Co. B	1,620	
80% of 1,500 profit made by Co. C	1,200	2,820
Company B:		
Raw Materials:		
80% of $500 profit made by Co. C		400
Goods in Process:		
80% of $1,000 profit made by Co. C		800
Finished Goods:		
80% of $1,300 profit made by Co. C		1,040
		$9,150

The unrealized profit is summarized by inventories as follows:

	Co. A's Inventory	*Co. B's Inventory*	*Total*
Raw Materials	$3,210	$ 400	$3,610
Goods in Process	880	800	1,680
Finished Goods	2,820	1,040	3,860
Total reserve at December 31, 1921			$9,150

After computing these adjustments for inter-company profits in inventories, the consolidated working papers may be drawn up. The working papers for cost of sales are prepared in the following form:

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED STATEMENT OF COST OF GOODS SOLD—WORKING PAPERS

For the Year Ending December 31, 1921

	Co. A	*Co. B*	*Co. C*	*Cost of Sales Adjustments* Dr.	Cr.	*Inter-Co. Eliminations*	*Consolidated Cost of Sales*
Materials, Inventory January 1, 1921	$ 40,000	$15,000	$15,000		$1,800(a)		$ 68,200
Purchases—Raw Materials	145,000	95,000	76,000			$170,000(A)	146,000
Total	185,000	110,000	91,000				214,200
Less Inventory, December 31, 1921	50,000	25,000	11,000	$3,610(b)			82,390
Materials Used	135,000	85,000	80,000				131,810
Direct Labor	85,000	65,000					150,000
Manufacturing Expense	70,000	40,000				3,000(B)	107,000
Total	290,000	190,000	80,000				388,810
Add Goods in Process, January 1, 1921	25,000	30,000			1,350(a)		53,650
Total	315,000	220,000	80,000				442,460
Deduct Goods in Process, December 31, 1921	55,000	25,000		1,680(b)			78,320
Cost of Goods Manufactured and Purchases Sold	260,000	195,000	80,000				364,140
Add Inventory of Finished Goods, January 1, 1921		30,000					30,000
Total	260,000	225,000	80,000				394,140
Deduct Inventory Finished Goods, December 31, 1921	45,000	50,000		3,860(b)			91,140
Cost of Goods Sold	$215,000	$175,000	$80,000				$303,000

The adjustments marked (a) eliminate the inter-company profit in the inventories at January 1, 1921. Since the inventories at that date are charged to cost of sales the unrealized profit is credited to cost of sales as a deduction; the offsetting debit is a charge against the holding company's surplus as of January 1, 1921, and will appear as adjustment (a) in the consolidated surplus working papers.

The adjustments marked (b) eliminate the inter-company profit in the inventories at December 31, 1921. Since these inventories are credited to cost of sales the unrealized profit is charged to cost of sales as a deduction; the offsetting credit sets up the reserve which will appear in the consolidated balance sheet.

Elimination (A) takes the inter-company purchases out of the purchases accounts; this elimination will be offset in the consolidated profit and loss statement working papers by elimination (A) taking the same amount out of sales.

Elimination (B) takes out of Company B's manufacturing expense the rent of equipment charged by Company A. This elimination will be offset in the consolidated profit and loss statement working papers by elimination (B) taking the rent income out of Company A's profit and loss account.

Since only one side of each adjustment and elimination appears in the working papers, it is useless to add these columns, as the addition is useful only as a means of proof on the trial balance basis.

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED PROFIT AND LOSS STATEMENT—WORKING PAPERS

For the Year Ending December 31, 1921

	Co. A	*Co. B*	*Co. C*	*Elim.*	*Consolidated P. & L.*
Gross Sales	$300,000	$225,000	$120,000	$170,000(A)	$475,000
Less Returned Sales and Allowances	3,000	2,000	1,000		6,000
Net Sales	297,000	223,000	119,000		469,000
Less Cost of Goods Sold	215,000	175,000	80,000		303,000
Gross Profit on Sales	82,000	48,000	39,000		166,000
Less Selling Expenses	23,000	22,000	15,000		60,000
Net Profit on Sales	59,000	26,000	24,000		106,000
Less General and Administrative Expenses	22,000	11,000	3,000		36,000
Net Profit on Operations	37,000	15,000	21,000		70,000
Add Miscellaneous Income:					
Rent of Equipment to Co. B.	3,000			3,000(B)	
Bond Interest from Co. C.		2,000		2,000(C)	
Total	40,000	17,000	21,000		70,000
Less Bond Interest Paid	6,000		2,500	2,000(C)	6,500
Net Profit for the Year	$34,000	$17,000	$18,500		$63,500
Minority Interests:					
Company B (10%)		1,700			
Company C (20%)			3,700		
Total					5,400
Holding Company's Earnings					$58,100

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED STATEMENT OF COST OF GOODS SOLD

For the Year Ending December 31, 1921 (*Exhibit A*)

Goods in Process, January 1, 1921		$ 53,650
Materials:		
Inventory, January 1, 1921	$ 68,200	
Add Purchases	146,000	
Total	214,200	
Deduct Inventory, December 31, 1921	82,390	
Materials Used	131,810	
Direct Labor	150,000	
Manufacturing Expense	107,000	388,810
Total		442,460
Deduct Goods in Process, December 31, 1921		78,320
Cost of Goods Manufactured		364,140
Add Inventory of Finished Goods, January 1, 1921		30,000
Total		394,140
Deduct Finished Goods Inventory, December 31, 1921		91,140
Cost of Goods Sold		303,000

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED PROFIT AND LOSS STATEMENT (*Exhibit B*)

For the Year Ending December 31, 1921

Gross Sales		$475,000
Less Returned Sales and Allowances		6,000
Net Sales		469,000
Less Cost of Goods Sold (Exhibit A)		303,000
Gross Profit on Sales		166,000
Less Selling Expenses		60,000
Net Profit on Sales		106,000
Less General and Administrative Expenses		36,000
Net Profit on Operations		70,000
Deduct Bond Interest Paid		6,500
Net Profit for the Year		$63,500
Distributed as follows:		
Minority interest of Company B	$ 1,700	
Minority interest of Company C	3,700	
Holding Company A	58,100	
	$63,500	

First illustration continued: Consolidated surplus statement.—Following is a summary of the surplus accounts of the three companies:

	Co. A	*Co. B*	*Co. C*
Surplus, January 1, 1921	$35,000	$25,000	$20,000
Add Profits of 1921	34,000	17,000	18,500
Surplus, December 31, 1921	$69,000	$42,000	$38,500

In studying the consolidated surplus statement working papers which follow, it should be remembered that Company A has taken up its 90 per cent of the profits of Company B of former years, these profits being included in its $35,000 surplus at January 1, 1921.

The $31,850.00 balance of the holding company's surplus, after eliminating the $3,150.00 unrealized profit at the beginning of the year, should agree with the surplus shown in the consolidated balance sheet of January 1, 1921. The subsidiary surplus accounts are dealt with in accordance with paragraph 2 *c* on page 112.

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED SURPLUS STATEMENT—WORKING PAPERS

For the Year Ending December 31, 1921

	Co. A	*Co. B*	*Co. C*	*Adjustments Dr.*	*Adjustments Cr.*	*Eliminations*	*Minority*	*Consolidated Surplus*
Surplus, January 1, 1921:								
Company A	$35,000							
Adjustment for inter-company profit in inventories at January 1, 1921					$3,150(a)			
Adjusted Surplus at January 1, 1921								$31,850
Company B		$25,000						
Minority 10%							$2,500	
Eliminate Co. A's 90%						$22,500		
Company C			$20,000					
Minority 20%							4,000	
Eliminate Co. A's 80%						16,000		
Add Profits for 1921 (Per Consolidated P. & L.)	34,000	17,000	18,500				5,400	58,100
Surplus, December 31, 1921	$69,000	$42,000	$38,500				$11,900	$89,950

Adjustment (a) is an offset to the two (a) eliminations of $1,800 and $1,350 in the consolidated cost of sales working papers. The $22,500 and $16,000 eliminations would be offset in the consolidated balance sheet working papers as eliminations from the investment accounts.

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED SURPLUS STATEMENT *(Exhibit C)*

For the Year Ending December 31, 1921

Surplus, January 1, 1921	$31,850
Add Holding Company's share of 1921 Profits (Exhibit B)	58,100
Surplus, December 31, 1921 (Per Consolidated Balance Sheet)	$89,950

Second illustration: Consolidated profit and loss and surplus statements.—This illustration will be based on the same facts as the first illustration. In addition it is assumed that both subsidiaries have paid dividends, which have been credited by Company A to the respective investment accounts. The holding company has also paid dividends. None of these dividends will appear in the profit and loss statements of the several companies, and hence the consolidated profit and loss statement will be the same as in the first illustration.

Following is a statement of the surplus accounts:

	Co. A	*Co. B*	*Co. C*
Surplus, January 1, 1921	$35,000	$25,000	$20,000
Profits, 1921	34,000	17,000	18,500
Total	69,000	42,000	38,500
Less Dividends Paid	6,000	4,500	3,000
Surplus, December 31, 1921	$63,000	$37,500	$35,500

The following consolidated surplus statement is prepared from the working papers on page 122.

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED SURPLUS STATEMENT

Year Ending December 31, 1921

Surplus, January 1, 1921	$31,850
Add Profits of 1921—Per Consolidated P. & L. Statement	58,100
Total	89,950
Less Dividends Paid	6,000
Surplus, December 31, 1921	$83,950

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED SURPLUS STATEMENT—WORKING PAPERS

For the Year Ending December 31, 1921

	Co. A	Co. B	Co. C	Adjustments Dr.	Adjustments Cr	Elim.	Minority	Surplus
Surplus, January 1, 1921:								
Company A	$35,000							
Adjustment for inter-company profit in inventories at January 1, 1921					$3,150(a)			
Adjusted surplus as at January 1, 1921								$31,850
Company B		$25,000						
Minority 10%							$2,500	
Eliminate Co. A's 90%						$22,500		
Company C			$20,000					
Minority 20%							4,000	
Eliminate Co. A's 80%						16,000		
Add Profits of 1921—Per Consolidated P. & L.	34,000	17,000	18,500				5,400	58,100
Total	69,000	42,000	38,500				11,900	89,950
Deduct Dividends Paid:								
Company A	6,000							6,000
Company B		4,500				4,050	450	
Company C			3,000			2,400	600	
Surplus, December 31, 1921	$63,000	$37,500	$35,500				$10,850	$83,950

Third illustration: Consolidated profit and loss and surplus statements.—This illustration is based on the same facts as the first illustration, with the further assumption that the holding company is carrying its investment accounts at cost, and is taking up subsidiary dividends as a credit to Profit and Loss. But since no dividends were paid during 1921, there will be no dividend figures in the profit and loss statements, and hence the consolidated profit and loss working papers will be the same as in the first two illustrations.

The consolidated surplus statement working papers will differ from the two preceding ones in this particular: the holding company has not taken up the profits of the subsidiaries and hence its surplus will not include these profits but will include the subsidiary dividends. Therefore the surplus accounts of the subsidiaries at the beginning of the period will be disposed of as follows:

a. Carry minority interest in present surplus to the minority column.
b. Eliminate holding company's proportion of subsidiary surplus at date of acquisition.
c. Carry to the consolidated surplus column the holding company's proportion of the increase or decrease in subsidiary surplus since acquisition.

In this illustration it will be assumed that Company B had a surplus of $20,000 at the date of acquisition. Since that date its profits have been $15,000 and its dividends have been $10,000. Company A has not taken up its share of the profits but has taken up its share of the dividends of prior years by credits to profit and loss.

In the preceding illustrations Company A's surplus was shown as $35,000 at January 1, and this balance included $13,500 (90 per cent of $15,000) profits of Company B taken up. In this illustration, under the assumption that Company A has taken up only $9,000 (90 per cent of $10,000) dividends, Company A's surplus will be $30,500 instead of $35,000. The surplus accounts of the other companies will be unchanged.

The consolidated surplus statement prepared from the following working papers will be exactly like the one in the first illustration, on page 121.

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED SURPLUS STATEMENT—WORKING PAPERS

For the Year Ending December 31, 1921

	Co. A	Co. B	Co. C	Adjustments Dr.	Adjustments Cr.	Elim.	Minority	Surplus
Surplus, January 1, 1921:								
Company A	$30,500							
Adjustment for inter-company profits in inventories at January 1, 1921					$3,150			
Adjusted Surplus								$27,350
Company B		$25,000						
Minority 10% of $25,000 surp. at Jan. 1							$2,500	
Elim. Co. A's 90% of 20,000 surp. at acquis.						$18,000		
Surplus 90% of 5,000 increase								4,500
Company C			$20,000					
Minority 20% of $20,000 surp. at Jan. 1							4,000	
Elim. Co. A's 80% of 20,000 surp. at acquis.						16,000		
Consolidated surplus at January 1, 1921								31,850
Profits of 1921—Per Consolidated P. & L.	34,000	17,000	18,500				5,400	58,100
Surplus, December 31, 1921	$64,500	$42,000	$38,500				$11,900	$89,950

Fourth illustration: Consolidated profit and loss statement.—This illustration will be based on the same facts as the third illustration, with the additional assumption that the three companies paid dividends during 1921 as follows:

Company A	$6,000
Company B	4,500
Company C	3,000

Company A has taken up its proportion of the subsidiary dividends by credits to profit and loss; it is carrying the investment accounts at cost.

The consolidated profit and loss statement working papers will be the same as in the first illustration, on page 118, down to Net Profit on Operations. The dividends are shown under Miscellaneous Income in the working papers on page 126.

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED PROFIT AND LOSS STATEMENT WORKING PAPERS—*Continued*

For the Year Ending December 31, 1921

	Co. A	*Co. B*	*Co. C*	*Elim.*	*Consolidated P. & L.*
Net Profit on Operations (as on page 118)	$37,000	$15,000	$21,000		$70,000
Add Miscellaneous Income:					
Rent of Equipment to Co. B	3,000			$3,000(B)	
Bond Interest from Co. C		2,000		2,000(C)	
Dividends Received:					
From Co. B (90% of $4,500)	4,050			4,050(D)	
From Co. C (80% of 3,000)	2,400			2,400(E)	
Total	46,450	17,000	21,000		70,000
Less Bond Interest Paid	6,000		2,500	2,000(C)	6,500
Net Profit for the Year	$40,450	$17,000	$18,500		$63,500
Minority interests in 1921 profits:					
Company A (10%)		$1,700			
Company B (20%)			$3,700		
Total					5,400
Holding Company's Earnings					$58,100

The reader is already familiar with eliminations (B) and (C). The eliminations (D) and (E) for dividends received are offset by eliminations of dividends paid, in the consolidated surplus statement working papers which follow.

The consolidated profit and loss statement prepared from these working papers will be the same as the one on page 119.

Fourth illustration continued: Consolidated surplus.—The consolidated surplus statement working papers will be the same as in the third illustration, on page 124, with the additional fact of the deduction of dividends.

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED SURPLUS STATEMENT WORKING PAPERS — *Continued*

For the Year Ending December 31, 1921

	Co. A	*Co. B*	*Co. C*	*Adjustments* *Dr.*	*Cr.*	*Elim.*	*Minority*	*Surplus*
Balances before deduction of dividends (as on page 124)	$64,500	$42,000	$38,500				$11,900	$89,950
Deduct Dividends Paid:								
Company A	6,000							6,000
Company B		4,500				$4,050(D)	450	
Company C			3,000			2,400(E)	600	
Surplus—December 31, 1921	$58,500	$37,500	$35,500				$10,850	$83,950

The consolidated surplus statement will be exactly like the one in the second illustration, on page 121.

Chapter XV

CONSOLIDATED PROFIT AND LOSS STATEMENT, SURPLUS STATEMENT AND BALANCE SHEET

COMBINED WORKING PAPERS FROM TRIAL BALANCES

Form of working papers.—When a single set of working papers is prepared from the trial balances of the holding company and the subsidiaries to obtain the consolidated figures for the cost of goods sold statement, the profit and loss statement, the surplus statement, and the balance sheet, the working papers should contain columns for the trial balance of each company, for adjustments, inter-company eliminations, manufacturing account, selling account (or the two latter may be combined in a single Cost of Sales column to save space), profit and loss, and balance sheet.

Outline of illustrations.—This chapter will contain three illustrations, divided into two groups, as follows:

Group I. Subsidiary profits and losses taken up on the holding company's books; dividends recorded as a credit to the Investment account.

First illustration: All dividends credited to investment account; hence balance at end of year represents book value at the beginning of year minus dividends received during the year, and plus goodwill.

Group II. Investment account carried at cost.

Second illustration: 100 per cent ownership. All stock acquired at beginning of period.

Third illustration: Less than 100 per cent ownership. Stock acquired prior to beginning of period.

First illustration.—This illustration is based on the same conditions as the second illustration in the preceding chapter. Ninety per cent of the stock of Company B was acquired prior to the beginning of the period, and 80 per cent of the stock of Company C was acquired at the beginning of the period. All subsidiary earnings and dividends have been recorded through the investment account; therefore at the beginning of the period the investment accounts represented book value plus goodwill.

During the year the holding company has taken up dividends by credits to the investment accounts but has not taken up the subsidiary profits for the year.

Following are the trial balances of the holding company and subsidiaries at December 31, 1921.

COMPANY A AND SUBSIDIARIES

TRIAL BALANCES—DECEMBER 31, 1921

Debits	*Co. A*	*Co. B*	*Co. C*
Cash	$16,450	$7,500	$22,500
Accounts Receivable	30,000	35,000	50,000
Inventories, January 1, 1921:			
Raw Materials	40,000	15,000	15,000
Goods in Process	25,000	30,000	
Finished Goods		30,000	
Co. B Current Account	10,000		
Co. C. Current Account		5,000	
Plant and Machinery	125,000		70,000
Investment in Stock of Co. B (90%)	90,450		
Investment in Stock of Co. C (80%)	57,600		
Bonds of Co. C		40,000	
Purchases, Raw Materials	145,000	95,000	76,000
Direct Labor	85,000	65,000	
Manufacturing Expense	70,000	40,000	
Returned Sales and Allowances	3,000	2,000	1,000
Selling Expenses	23,000	22,000	15,000
General and Administrative Expenses	22,000	11,000	3,000
Bond Interest Paid	6,000		2,500
Dividends Paid	6,000	4,500	3,000
	$754,500	$402,000	$258,000
Credits			
Capital Stock	$200,000	$75,000	$50,000
Surplus, January 1, 1921	35,000	25,000	20,000
Bonds Payable	100,000		50,000
Reserve for Depreciation	11,500		3,000
Accounts Payable	55,000	20,000	10,000
Notes Payable	50,000	45,000	
Company A Current		10,000	
Company B Current			5,000
Sales	300,000	225,000	120,000
Rent of Equipment to Co. B	3,000		
Bond Interest Received from Co. C		2,000	
	$754,500	$402,000	$258,000

In the following consolidated working papers the adjustments and inter-company eliminations are cross-referenced by letters to facilitate tracing offsetting items.

COMPANY A AND SUBSIDIARIES

CONSOLIDATED WORKING PAPERS

For the Year Ending December 31, 1921

Debits	*Co. A*	*Co. B*	*Co. C*	*Adjustments Dr.*	*Adjustments Cr.*	*Eliminations*	*Cost of Sales*	*P. & L.*	*Balance Sheet*
Cash	$16,450	$7,500	$22,500						$46,450
Accounts Receivable	30,000	35,000	50,000						115,000
Inventories, January 1, 1921:									
Raw Materials	40,000	15,000	15,000		$1,800(b)		$68,200		
Goods in Process	25,000	30,000			1,350(b)		53,650		
Finished Goods		30,000					30,000		
Co. B Current	10,000					$10,000(A)			
Co. C Current		5,000				5,000(B)			
Plant and Machinery	125,000		70,000						195,000
Investment in Stock of Co. B (90%)	90,450								
Eliminate book value at January 1, 1921 less year's dividends out of January first surplus:									
Capital stock: 90% of $75,000						67,500(C)			
Surplus: 90% of 20,500						18,450(D)			
Goodwill									4,500 G
Investment in Stock of Co. C (80%)	57,600								
Eliminate book value at January 1, 1921 less year's dividends out of January first surplus:									
Capital stock: 80% of $50,000						40,000(E)			
Surplus: 80% of 17,000						13,600(F)			
Goodwill									4,000 G
Bonds of Company C		40,000							40,000
Purchases—Raw Materials	145,000	95,000	76,000			170,000(G)	146,000		
Direct Labor	85,000	65,000					150,000		

Manufacturing Expense	$70,000	$40,000				$3,000(H)	$107,000		
Returned Sales and Allowances	3,000	2,000	$1,000					$6,000	
Selling Expenses	23,000	22,000	15,000					60,000	
General and Administrative Expenses	22,000	11,000	3,000					36,000	
Bond Interest Paid:									
Co. A	6,000							6,000	
Co. C			2,500			2,000(I)		500	
Dividends Paid:									
Co. A	6,000								$6,000 S
Co. B		4,500			$4,500(c)				
Co. C			3,000		3,000(d)				
	$754,500	$402,000	$258,000						
Total Debits to Nominal Accounts	$419,000	$310,000	$112,500						
Inventories—December 31, 1921				$261,000(a)					261,000
				$261,000	$10,650	$329,550			
Total Debits to Cost of Sales							554,850		
Less Credits to Cost of Sales—per contra							251,850		
Cost of Goods Sold—to P. & L.							$303,000	303,000	
Total Debits to P. & L. Deducted contra								$411,500	
									$671,950

CONSOLIDATED WORKING PAPERS—*Continued*

Credits	*Co. A*	*Co. B*	*Co. C*	*Adjustments Dr.*	*Adjustments Cr.*	*Eliminations*	*Cost of Sales*	*P. & L.*	*Balance Sheet*
Adjustment columns forward...				$261,000	$10,650				
Capital Stock:									
Company A	$200,000								$200,000
Company B		$75,000							
Minority 10%									7,500M
Eliminate 90%						$67,500(C)			
Company C			$50,000						
Minority 20%									10,000M
Eliminate 80%						40,000(E)			
Surplus:									
Company A	35,000								
Adjustment for inter-company profit in Jan. 1 inventories				3,150(b)					
Adjusted Surplus, Jan. 1									31,850 S
Company B		25,000		4,500(c)					
Minority 10% of $20,500									2,050M
Eliminate 90% of 20,500						18,450(D)			
Company C			20,000	3,000(d)					
Minority 20% of $17,000									3,400M
Eliminate 80% of 17,000						13,600(F)			
Bonds Payable	100,000		50,000						150,000
Reserve for Depreciation	11,500		3,000						14,500
Accounts Payable	55,000	20,000	10,000						85,000
Notes Payable	50,000	45,000							95,000
Co. A Current		10,000				10,000(A)			
Co. B Current			5,000			5,000(B)			
Sales	300,000	225,000	120,000			170,000(G)		$475,000	
Rent of Equipment to Co. B	3,000					3,000(H)			
Bond Interest Received from Co. C		2,000				2,000(I)			
	$754,500	$402,000	$258,000						

Inventories, December 31, 1921:									
Raw Materials	$50,000	$25,000	$11,000	$3,610(e)	$86,000(a)		$82,390		
Goods in Process	55,000	25,000		1,680(e)	80,000(a)		78,320		
Finished Goods	45,000	50,000		3,860(e)	95,000(a)		91,140		
Reserve for Inter-Company Profit in December 31, 1921, inventories					9,150(e)				$9,150 R
Total Credits to Nominal Accounts (including Dec. 31 inventories)	453,000	327,000	131,000						
Less Debits to Nominal Accounts	419,000	310,000	112,500						
Net Profit of Separate Companies	$34,000	$17,000	$18,500						
Minority interests		$1,700	$3,700						
				$280,800	$280,800	$329,550			
Total Credits to Cost of Sales—deducted contra							$251,850		
Total Credits to Profit and Loss								475,000	
Less Total Debits to Profit and Loss—per contra								411,500	
Net Profit for the Year								63,500	
Minority Interest in Co. B							$1,700		1,700M
Minority Interest in Co. C							3,700	5,400	3,700M
Holding company's share of net profit									58,100 S
									$671,950

Explanation of working papers.—These working papers were prepared in the following manner: The trial balance figures were entered, leaving room for eliminations after the investment accounts and after the capital stock and surplus accounts. The trial balance columns were then added to detect any possible errors in copying figures from the trial balances to the working papers.

The inventories at December 31, 1921, were entered by adjustment (a) by a debit to Inventories on the debit sheet and a credit to Cost of Sales on the credit sheet. The inventories were listed in detail on the credit side in the columns of the several companies, so that they could be readily included in the total credits to the nominal accounts of each company in determining its profit. The debit to Inventories was carried to the consolidated balance sheet column. In drawing up the consolidated balance sheet the detail of the inventories can be obtained from the credit sheet.

An adjustment was made for inter-company profits in inventories at January 1, 1921, by adjustment (b) debiting Company A's surplus and crediting the inventories, thus reducing the charge to cost of sales for the opening inventories.

The dividends paid by Company B and Company C were transferred to the respective surplus accounts by adjustments (c) and (d). These entries are made because the holding company has taken up these dividends by credits to the investment accounts. Since it is following this method of accounting, eliminations will be made on the basis of present book values; i.e., surplus at January 1, 1921, less dividends paid in 1921. The investment accounts represent book values at January 1, 1921, less dividends received; therefore the surplus elimination should be on the basis of January 1, 1921 surplus less dividends paid.

A reserve for inter-company profits in inventories at December 31, 1921, was created by adjustment (e) charging cost of sales (as a reduction of the inventories to be credited to cost of sales) and crediting the reserve, which was carried to the consolidated balance sheet column.

All inter-company accounts were eliminated. These eliminations may be traced by the letters.

All items affecting cost of sales were carried to the cost of sales column after making deductions as indicated by the adjustments and eliminations. Items affecting profit and loss

and items to appear in the consolidated balance sheet were carried to their respective columns.

Trial balance nominal account debits were added and deducted from trial balance nominal account credits (including inventories) to determine the profit of each company and the minority interests in profits.

The adjustment and elimination columns were footed to see that they balanced.

On the debit sheet the total of the consolidated cost of sales column was determined; the total of the credits to cost of sales was determined and carried over to the debit sheet where it was deducted from the total debits to obtain the net cost of sales of $303,000. This amount was carried to the debit profit and loss column.

On the credit sheet the total of the profit and loss column was determined; the total of the debits to profit and loss was determined and carried over to the credit sheet where it was deducted from the total credits to ascertain the net profit for the year. The two minority interests were deducted and carried to the consolidated balance sheet column, and the remaining net profit, applicable to the holding company, was carried to the consolidated balance sheet column.

The two consolidated balance sheet columns were footed.

Consolidated statements.—The consolidated cost of goods sold statement prepared from these working papers will be exactly like the one on page 118 of Chapter XIV, and will show $303,000 as the cost of goods sold during the year. The consolidated profit and loss statement will be identical with the one on page 119 of Chapter XIV, and will show $58,100 as the consolidated net profit. The consolidated surplus statement will be a duplicate of the one on page 121 and will show $83,950 as the consolidated surplus. This is the same surplus which appears in the following consolidated balance sheet.

The following data are summarized from the working papers for use in the consolidated balance sheet:

	Minority in B	*Minority in C*	*Consolidated Surplus*
Surplus, January 1, 1921—less dividends	$2,050	$3,400	$25,850
Profits of 1921	1,700	3,700	58,100
Surplus, December 31, 1921	3,750	7,100	$83,950
Minority Interests in Capital Stock	7,500	10,000	
Total Minority Interests	$11,250	$17,100	

COMPANY A AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

December 31, 1921

Assets

Fixed Assets:			
Plant and Machinery	$195,000		
Less Reserve for Depreciation	14,500	$180,500	
Goodwill		8,500	$189,000
Current Assets:			
Inventories:			
Raw Materials	$86,000		
Goods in Process	80,000		
Finished Goods	95,000	261,000	
Less Reserve for Inter-Company Profit		9,150	251,850
Accounts Receivable			115,000
Cash			46,450	413,300
				$602,300

Liabilities

Fixed Liabilities:			
Bonds Payable		$150,000	
Less Treasury Bonds		40,000	$110,000
Current Liabilities:			
Accounts Payable		85,000	
Notes Payable		95,000	180,000
Minority Interests:			
In Company B (10%)		11,250	
In Company C (20%)		17,100	28,350
Capital:			
Capital Stock		200,000	
Surplus		83,950	283,950
			$602,300

Second illustration.—In this illustration, which is taken from a recent Ohio C. P. A. examination, the holding company acquired all of the stock of the subsidiaries at the beginning of the period. No profits have been taken up; dividends have been credited to Dividends Received to be transferred to Surplus at the end of the period. A consolidated profit and loss statement, surplus statement and balance sheet are to be prepared from the following trial balances at the end of 1919.

Debits	*Cleveland Mfg. Co.*	*Cincinnati Mfg. Co.*	*Columbus Mfg. Co.*
Cash	$150,000	$ 50,000	$110,000
Accounts Receivable	650,000	210,000	400,000
Notes Receivable	300,000	50,000	50,000
Raw Materials Purchased	600,000	380,000	490,000
Labor	430,000	350,000	350,000
Manufacturing Expenses	220,000	170,000	160,000
Selling Expenses	100,000	60,000	100,000
Administrative Expenses	50,000	30,000	40,000
Plant and Machinery	1,000,000	600,000	800,000
Dividends Paid	450,000	100,000	200,000
Capital Stock Owned:			
Cincinnati Mfg. Co	1,000,000		
Columbus Mfg. Co	1,500,000		
Inventory, January 1, 1919	150,000	100,000	150,000
	$6,600,000	$2,100,000	$2,850,000
Credits			
Accounts Payable	$150,000	$105,000	$360,000
Notes Payable	50,000	95,000	90,000
Sales	1,500,000	1,100,000	1,200,000
Dividends Received	300,000		
Capital Stock	4,500,000	500,000	800,000
Surplus, January 1, 1919	100,000	300,000	400,000
	$6,600,000	$2,100,000	$2,850,000

The inventories at December 31, 1919, were as follows:

Cleveland Company	$300,000
Cincinnati Company	150,000
Columbus Company	200,000

Provide 10 per cent depreciation on total plant and machinery.

Notes payable of the Cincinnati Manufacturing Co. amounting to $95,000 and of the Columbus Manufacturing Co. amounting to $90,000 are for money advanced by the Cleveland Manufacturing Co. and are included in notes receivable of the Cleveland Manufacturing Co.

The inventory of the Columbus Manufacturing Co. includes goods purchased from the Cleveland Manufacturing Co. on which the latter company made a profit of $25,000.

The accounts receivable of the Cleveland Manufacturing Co. include $200,000 due from the Columbus Manufacturing Co. for goods shipped during the year.

The entire capital stocks of the Cincinnati and Columbus companies were acquired on January 1, 1919, at the cost as shown by the books of the Cleveland Manufacturing Co.

THE CLEVELAND MANUFACTURING COMPANY AND SUBSIDIARIES

CONSOLIDATED WORKING PAPERS

Year Ending December 31, 1919

Debits	*Cleveland*	*Cincinnati*	*Columbus*	*Adjustments* Dr.	Cr.	*Eliminations*	*Cost of Sales*	*P. & L.*	*Balance Sheet*	
Cash	$150,000	$ 50,000	$110,000						$ 310,000	
Accounts Receivable	650,000	210,000	400,000			$200,000(A)			1,060,000	
Notes Receivable	300,000	50,000	50,000			185,000(B)			215,000	
Raw Material Purchased	600,000	380,000	490,000			200,000(C)	$1,270,000			
Labor	430,000	350,000	350,000				1,130,000			
Manufacturing Expenses	220,000	170,000	160,000				550,000			
Selling Expenses	100,000	60,000	100,000					$260,000		
Administrative Expenses	50,000	30,000	40,000					120,000		
Plant and Machinery	1,000,000	600,000	800,000						2,400,000	
Dividends Paid	450,000	100,000	200,000			300,000(D)			450,000	S
Capital Stock Owned:										
Cincinnati Mfg. Co. (100%) Cost	1,000,000									
Eliminate book value at acquisition:										
Capital stock						500,000(E)				
Surplus						300,000(F)				
Goodwill									200,000	G
Columbus Mfg. Co. (100%) Cost	1,500,000									
Eliminate book value at acquisition:										
Capital stock						800,000(G)				
Surplus						400,000(H)				
Goodwill									300,000	G
Inventories—January 1, 1919	150,000	100,000	150,000				400,000			
	$6,600,000	$2,100,000	$2,850,000							

Inventories—December 31, 1919				$650,000(a)					$650,000
Depreciation	$100,000	$60,000	$80,000	$240,000(c)			$240,000		
Total Debits to Nominal Accounts	$1,650,000	$1,150,000	$1,370,000						
				$890,000		0 $2,885,000			
Total Debits to Cost of Sales							3,590,000		
Less Total Credits to Cost of Sales—per contra							625,000		
Cost of Sales—to P. & L.							$2,965,000	2,965,000	
Total Debits to Profit and Loss—deducted contra								$3,345,000	
									$5,585,000

THE CLEVELAND MANUFACTURING COMPANY AND SUBSIDIARIES

CONSOLIDATED WORKING PAPERS—*Continued*

Credits	*Cleveland*	*Cincinnati*	*Columbus*	*Adjustments Dr.*	*Adjustments Cr.*	*Eliminations*	*Cost of Sales*	*P. & L.*	*Balance Sheet*
Adjustment column totals forward				$890,000					
Accounts Payable	$150,000	$105,000	$360,000			$200,000(A)			$415,000
Notes Payable	50,000	95,000	90,000			185,000(B)			50,000
Sales	1,500,000	1,100,000	1,200,000			200,000(C)		$3,600,000	
Dividends Received	300,000					300,000(D)			
Capital Stock:									
Cleveland Mfg. Co.	4,500,000								4,500,000
Cincinnati Mfg. Co.		500,000							
Elim. H. C. 100%						500,000(E)			
Columbus Mfg. Co.			800,000						
Elim. H. C. 100%						800,000(G)			
Surplus—January 1, 1919:									
Cleveland Mfg. Co.	100,000								100,000 S
Cincinnati Mfg. Co.		300,000							
Elim. H. C. 100% of $300,000 at acquisition						300,000(F)			
Columbus Mfg. Co.			400,000						
Elim. H. C. 100% of $400,000 at acquisition						400,000(H)			
	$6,600,000	$2,100,000	$2,850,000						

Inventories, Dec. 31, 1919	$300,000	$150,000	$200,000	$25,000(b)	$650,000(a)		$625,000		
Reserve for Inter-Co. profit in Dec. 31 inventories					$ 25,000(b)				$ 25,000 R
Reserve for Depreciation					240,000(c)				240,000
Total Credits to Nominal Accounts	2,100,000	1,250,000	1,400,000						
Less Debits to Nominal Accounts (contra)	1,650,000	1,150,000	1,370,000						
Net Profit per books	$450,000	$100,000	$30,000						
				$915,000	$915,000	$2,885,000			
Total Credits to Cost of Sales—deducted contra							$625,000		
Total Credits to Profit and Loss								3,600,000	
Less Debits to Profit and Loss (per contra)								3,345,000	
Net Profit—to Surplus								$255,000	255,000 S
									$5,585,000

The inter-company sales and purchases may have been more than $200,000 but the only information as to these transactions is contained in the statement that there were $200,000 of inter-company receivables at the end of the year for goods sold during the year.

THE CLEVELAND MANUFACTURING COMPANY
AND SUBSIDIARIES (*Exhibit A*)

CONSOLIDATED PROFIT AND LOSS STATEMENT

For the Year Ending December 31, 1919

Sales		$3,600,000
Less Cost of Goods Sold:		
Inventory, January 1, 1919	$ 400,000	
Purchases	1,270,000	
Labor	1,130,000	
Manufacturing Expense	550,000	
Depreciation—Plant and Machinery	240,000	
Total	$3,590,000	
Less Inventory, December 31, 1919	625,000	2,965,000
Gross Profit on Sales		$635,000
Less Selling Expenses		260,000
Net Profit on Sales		$375,000
Less Administrative Expenses		120,000
Net Profit for the Year		$255,000

THE CLEVELAND MANUFACTURING COMPANY
AND SUBSIDIARIES (*Exhibit B*)

CONSOLIDATED SURPLUS STATEMENT

For the Year Ending December 31, 1919

Surplus—January 1, 1919	$100,000
Add Profits—1919	255,000
Total	$355,000
Deduct Dividends paid in 1919	450,000
Deficit—December 31, 1919	$95,000

THE CLEVELAND MANUFACTURING COMPANY
AND SUBSIDIARIES (*Exhibit C*)

CONSOLIDATED BALANCE SHEET

December 31, 1919

Assets

Fixed Assets:			
Plant and Machinery	$2,400,000		
Less Reserve for Depreciation	240,000	$2,160,000	
Goodwill		500,000	$2,660,000
Current Assets:			
Inventories	$650,000		
Less Reserve for Inter-Company Profit	25,000	$625,000	
Accounts Receivable		1,060,000	
Notes Receivable		215,000	
Cash		310,000	2,210,000
			$4,870,000

Liabilities

Capital:			
Capital Stock		$4,500,000	
Less Deficit (Exhibit B)		95,000	$4,405,000
Current Liabilities:			
Accounts Payable		415,000	
Notes Payable		50,000	465,000
			$4,870,000

Third illustration.—This illustration is based on the same data as the second illustration, with the following changes:

1. The holding company owns only 90 per cent of the stock of each company. This change will introduce the feature of minority interests.

2. The holding company acquired its stock interests at January 1, 1918. This change will introduce two features:

a. Adjustments will have to be made for inter-company profit in inventories at January 1, 1919, which were:

(1). In Cincinnati inventories, $20,000 added on sales by Columbus.

(2). In Cleveland inventories, $15,000 added on sales by Cincinnati. (See page 148).

THE CLEVELAND MANUFACTURING COMPANY AND SUBSIDIARIES

CONSOLIDATED WORKING PAPERS

For the Year Ending December 31, 1919

Debits	*Cleveland*	*Cincinnati*	*Columbus*	*Adjustments Dr.*	*Adjustments Cr.*	*Eliminations*	*Cost of Sales*	*P. & L.*	*Balance Sheet*
Cash	$120,000	$50,000	$110,000						$ 280,000
Accounts Receivable	650,000	210,000	400,000			$200,000 (A)			1,060,000
Notes Receivable	300,000	50,000	50,000			185,000 (B)			215,000
Raw Materials Purchased	600,000	380,000	490,000			200,000 (C)	$1,270,000		
Labor	430,000	350,000	350,000				1,130,000		
Manufacturing Expenses	220,000	170,000	160,000				550,000		
Selling Expenses	100,000	60,000	100,000					$260,000	
Administration Expenses	50,000	30,000	40,000					120,000	
Plant and Machinery	1,000,000	600,000	800,000						2,400,000
Dividends Paid:									
Cleveland	450,000								450,000 S
Cincinnati		100,000				90,000 (D)			10,000M
Columbus			200,000			180,000 (D)			20,000M
Capital Stock Owned:									
Investment in Cincinnati Stock (90%) Cost	1,000,000								
Eliminate book value at acquisition:									
Capital stock: 90% of $500,000						450,000 (E)			
Surplus: 90% of 160,000						144,000 (F)			
Goodwill									406,000 G

Investment in Columbus Stock (90%) Cost	$1,500,000								
Eliminate book value at acquisition:									
Capital stock: 90% of $800,000						$720,000 (G)			
Surplus: 90% of 500,000						450,000 (H)			
Goodwill									$330,000 G
Inventories—January 1, 1919	150,000	$100,000	$150,000		$31,500(b)		$368,500		
	$6,570,000	$2,100,000	$2,850,000						
Inventories—December 31, 1919				$650,000(a)					650,000
Depreciation of Plant and Machinery	100,000	60,000	80,000	240,000(d)			240,000		
Total Debits to Nominal Accounts	$1,650,000	$1,150,000	$1,370,000						
				$890,000	$31,500	$2,619,000			
Total Debits to Cost of Sales							3,558,500		
Less Credits to Cost of Sales—per contra							627,500		
Cost of Sales—to P. & L.							$2,931,000	2,931,000	
Total Debits to Profit and Loss—Deducted Contra								$3,311,000	
									$5,821,000

THE CLEVELAND MANUFACTURING COMPANY AND SUBSIDIARIES

CONSOLIDATED WORKING PAPERS—*Continued*

Credits	*Cleveland*	*Cincinnati*	*Columbus*	*Adjustments Dr.*	*Adjustments Cr.*	*Eliminations*	*Cost of Sales*	*P. & L.*	*Balance Sheet*
Adjustment column totals forward				$890,000	$31,500				
Accounts Payable	$150,000	$105,000	$360,000			$200,000A			$415,000
Notes Payable	50,000	95,000	90,000			185,000B			50,000
Sales	1,500,000	1,100,000	1,200,000			200,000C		$3,600,000	
Dividends Received	270,000					270,000D			
Capital Stock:									
Cleveland	4,500,000								4,500,000
Cincinnati		500,000							
Elim. H. C. 90%						450,000E			
Minority 10%									50,000M
Columbus			800,000						
Elim. H. C. 90%						720,000G			
Minority 10%									80,000M
Surplus—January 1, 1919:									
Cleveland	100,000								
Adjustment for inter-company profit in Jan. 1 inventories (90% of $35,000)				31,500(b)					
Adjusted Surplus									68,500S
Cincinnati		300,000							
Minority 10% of $300,000 sur. at Jan. 1									30,000M
Elim. H. C. 90% of 160,000 sur. at acquis.						144,000F			
H. C. Surp. 90% of $140,000 increase									126,000S
Columbus			$400,000						
Minority 10% of $400,000 sur. at Jan. 1									$40,000M
Elim. H. C. 90% of 500,000 sur. at acquis.						$450,000H			
H. C. Surp. 90% of $100,000 decrease									90,000*S
	$6,570,000	$2,100,000	$2,850,000						
Inventories—December 31, 1919	$300,000	$150,000	$200,000	$22,500(c)	$650,000(a)		$627,500		
Reserve for 90% of Inter-company profit in December 31, 1919, Inventories					22,500(c)				22,500 R
Reserve for Depreciation					240,000(d)				240,000
Total Credits to Nominal Accounts	2,070,000	1,250,000	1,400,000						
Less Debits to Nominal Accounts (per contra)	1,650,000	1,150,000	1,370,000						
Net Profit per books	$420,000	$100,000	$30,000						
Minority Interests in 1919 Profits		$10,000	$3,000						
				$944,000	$944,000	$2,619,000			
Total Credits to Cost of Sales—deducted contra							$627,500		
Total Credits to Profit and Loss								3,600,000	
Less Debits to Profit and Loss (per contra)								3,311,000	
Net Profit for the Year								289,000	
Minority Interest:									
Cincinnati Mfg. Co. (10%)							10,000		10,000M
Columbus Mfg. Co. (10%)							3,000	13,000	3,000M
Holding Company's Share of Net Profit								$276,000	276,000 S
									$5,821,000

b. The eliminations from the investment accounts and the subsidiary surplus accounts will be based on book values at a date prior to the beginning of the period, and hence on surplus amounts different from those shown in the trial balances, which are the surplus balances at the first of the year.

Since the holding company has not taken up profits, losses and dividends by entries in the investment accounts, the balances represent the cost at January 1, 1918. At that date the Cincinnati Manufacturing Company had a surplus of $160,000 and the Columbus Manufacturing Company had a surplus of $500,000.

Since the holding company did not own all of the stock of the subsidiaries during the year, the dividends received were only 90 per cent of the amounts paid by the subsidiaries, and hence in the following working papers the dividends received from the Cincinnati Company appear in the trial balance at $90,000 instead of $100,000, and the dividends received from the Columbus Company appear at $180,000 instead of $200,000, a total reduction of $30,000. The holding company's cash is correspondingly reduced from $150,000 to $120,000.

THE CLEVELAND MANUFACTURING COMPANY
AND SUBSIDIARIES (*Exhibit A*)

CONSOLIDATED PROFIT AND LOSS STATEMENT

For the Year Ending December 31, 1919

Sales		$3,600,000
Deduct Cost of Goods Sold:		
Inventory, January 1, 1919	$ 368,500	
Purchases	1,270,000	
Labor	1,130,000	
Manufacturing Expense	550,000	
Depreciation — Plant and Machinery	240,000	
Total	3,558,500	
Less Inventory, December 31, 1919	627,500	2,931,000
Gross Profit on Sales		669,000
Less Selling Expenses		260,000
Net Profit on Sales		409,000
Less Administrative Expenses		120,000
Net Profit for the Year		$ 289,000
For Minority Stockholders of Cincinnati Mfg. Co.	$ 10,000	
For Minority Stockholders of Columbus Mfg. Co.	3,000	
For Cleveland Mfg. Co	276,000	
	$289,000	

Before preparing the consolidated surplus statement, it is necessary to assemble the various elements of the consolidated surplus at January 1, 1919.

Cleveland Mfg. Co. surplus after adjustment for inter-company profit in inventories at January 1, 1919	$68,500
Add holding company's 90% of increase in Cincinnati Mfg. Co.'s surplus since acquisition	126,000
Total	194,500
Deduct holding company's 90% of decrease in Columbus Mfg. Co.'s surplus since acquisition	90,000
Adjusted surplus as at January 1, 1919	$104,500

THE CLEVELAND MANUFACTURING COMPANY
AND SUBSIDIARIES (*Exhibit B*)

CONSOLIDATED SURPLUS STATEMENT

For the Year Ending December 31, 1919

Surplus, January 1, 1919	$104,500
Add Profits for 1919 (Exhibit A)	276,000
Total	380,500
Deduct Dividends Paid	450,000
Deficit, December 31, 1919	$69,500

Before preparing the consolidated balance sheet it is desirable to assemble the elements of the minority interests:

	Cincinnati	*Columbus*
Capital stock	$50,000	$80,000
Surplus, January 1, 1919	30,000	40,000
Profits, 1919	10,000	3,000
Total	90,000	123,000
Less Dividends paid in 1919	10,000	20,000
Minority Interests, at December 31, 1919	$80,000	$103,000

THE CLEVELAND MANUFACTURING COMPANY
AND SUBSIDIARIES (*Exhibit C*)

CONSOLIDATED BALANCE SHEET

December 31, 1919

Assets			
Fixed Assets:			
Goodwill		$736,000	
Plant and Machinery	$2,400,000		
Less Reserve for Depreciation	240,000	2,160,000	$2,896,000
Current Assets:			
Inventories	650,000		
Less Reserve for Inter-Company Profit	22,500	627,500	
Accounts Receivable		1,060,000	
Notes Receivable		215,000	
Cash		280,000	2,182,500
			$5,078,500
Liabilities			
Current Liabilities:			
Accounts Payable		$ 415,000	
Notes Payable		50,000	$ 465,000
Minority Interests:			
Cincinnati Mfg. Co. (10%)		80,000	
Columbus Mfg. Co. (10%)		103,000	183,000
Capital:			
Capital Stock		4,500,000	
Less Deficit (Exhibit B)		69,500	4,430,500
			$5,078,500

APPENDIX A

PROBLEMS

Problem 1.—Three-fourths of the capital stock of Company A and two-thirds of the capital stock of Company B is owned by the holding company C. Company C purchased the above stock of Company A at 150 in February, 1905, on the basis of the balance sheet given below, dated January 1, 1905.

Assets		*Liabilities*	
Real Estate, Plant, etc.	$100,000	Capital Stock	$150,000
Inventory, Merchandise	100,000	Surplus	75,000
Accounts Receivable	75,000	Bills Payable	75,000
Cash	25,000		
	$300,000		$300,000

During the year 1905 Company A made a net profit after providing for depreciation, bad debts, etc., of $5,000, and the directors of Company A declare and pay a dividend of 10 per cent as of February 15, 1906.

The stock of Company B owned by Company C was purchased in March, 1905, at 125, on the basis of the balance sheet below, dated January 1, 1905.

Assets		*Liabilities*	
Real Estate, Plant, etc.	$450,000	Capital Stock	$500,000
Patents	50,000	Bonded Indebtedness	200,000
Inventory, Merchandise	200,000	Accounts Payable	62,500
Accounts Receivable	150,000	Surplus	125,000
Cash	37,500		
	$887,500		$887,500

During the year 1905 Company B made a net profit of $50,000 after making all necessary provision for bad debts and for depreciation on plant, machinery and patents. The directors of Company B declare and pay a dividend of 8 per cent as of February 14, 1906.

Draw up all the necessary entries in respect to the purchase of the stock of the two companies, their earnings and dividends, as they should appear on the books of Company C, the holding company.

Problem 2.—On January 1, 1910, X Y Z Company acquired the entire capital stock of the P Q Company, consisting of 1,000 shares of par value of $100 each, for which was paid the sum of $150,000. After the transaction was recorded on the books of the X Y Z Company, the balance sheets of the two companies were as follows:

	X Y Z Company		*P Q Company*	
Real Estate	$ 50,000		$25,000	
Buildings, Plant and Equipment	75,000		45,000	
Goodwill	25,000			
Investment in P Q Company	150,000			
Inventories	80,000		20,000	
Accounts Receivable	70,000*		85,000	
Accounts Payable		$50,000		$50,000*
Loans		50,000		
Capital Stock		250,000		100,000
Surplus		100,000		25,000
	$450,000	$450,000	$175,000	$175,000

*Includes account of $15,000 due by P Q Company to X Y Z Company.

Prepare a consolidated balance sheet.

Problem 3.—Company A purchased on January 1, 1917, the entire capital stock of Company B at $175 per share, and the entire stock of Company C at $80 per share. There are no inter-company accounts or inventories.

You are handed the balance sheets as understated, at June 30, 1917, and are requested to prepare a consolidated balance sheet of the A Company and its subsidiaries at that date.

BALANCE SHEET—COMPANY A

Property and goodwill	$850,000	Capital stock	$2,250,000
Stock of subsidiary companies	1,500,000	Current liabilities	150,000
Current assets	700,000	Surplus, January 1	525,000
		Undivided profits for half year	125,000
	$3,050,000		$3,050,000

BALANCE SHEET—COMPANY B

Property and goodwill	$650,000	Capital stock	$400,000
Current assets	60,000	Current liabilities	10,000
		Surplus, January 1	200,000
		Undivided profits for half year	100,000
	$710,000		$710,000

BALANCE SHEET—COMPANY C

Property (as appraised January 1, 1917)	$1,130,000	Capital stock	$1,000,000
Current assets	180,000	Current liabilities	240,000
		Surplus, January 1	30,000
		Undivided profits for half year	40,000
	$1,310,000		$1,310,000

Problem 4.—In the process of consolidating several competing establishments, Corporation A, the holding company, acquires $98,000 out of a total of $100,000 of the capital stock of Company B. At the time of the purchase the balance sheet of Company B showed surplus and undivided profits of $50,000. Company A bought the stock of B at 200 per cent. Almost immediately after the purchase Company B declared and paid a cash dividend of 25 per cent.

In what ways would the payment of this dividend affect (a) the balance sheet of B; (b) the balance sheet of A; (c) the consolidated balance sheet of A and its subsidiary companies?

Give reasons for your answer.

Problem 5.—Prepare a consolidated balance sheet with the use of the data contained below:

COMPANY A (Holding Company)

BALANCE SHEET

December 31, 1913

Assets			*Liabilities*	
Investment in other companies at cost:			Capital Stock	$2,000,000
B (75% interest)	$1,000,000		Collateral Trust 5% Notes	1,000,000
C (70% interest)	750,000		Surplus	1,000,000
D (80% interest)	850,000	$2,600,000		
Other Sundry Assets		1,400,000		
		$4,000,000		$4,000,000

NOTE: As indicated above, the Holding Company has not recognized in its books the increase or decrease in the value (represented in profits and losses) of the investments in sub-

sidiaries, except that dividends received from time to time have been carried to surplus account.

The dates as of which the interests in the various companies were acquired are as follows:

B—January 1, 1910
C—July 1, 1908
D—June 30, 1912

COMPANY B

BALANCE SHEET

December 31, 1913

Assets		*Liabilities*		
Fixed Assets	$500,000	Capital Stock		$600,000
Current Assets	500,000	Current Liabilities		100,000
Deferred Charges	100,000	Surplus:		
		Balance 1/1/10	$100,000	
		Profits Since	500,000	
			600,000	
		Dividends	200,000	400,000
	$1,100,000			$1,100,000

COMPANY C

BALANCE SHEET

December 31, 1913

Assets			*Liabilities*	
Fixed Assets		$700,000	Capital Stock	$800,000
Current Assets		250,000	Current Liabilities	300,000
Deferred Charges		50,000		
Deficiency Account:				
Balance 1/1/1906	$250,000			
Dividends, Dec. 1, 1913	500,000			
	750,000			
*Profits from 1/1/1906	650,000	100,000		
		$1,100,000		$1,100,000

* It can be assumed that there was no fluctuation of profits as between months.

COMPANY D

BALANCE SHEET

December 31, 1913

Assets		*Liabilities*		
Fixed Assets	$500,000	Capital Stock		$800,000
Current Assets	500,000	Current Liabilities		100,000
Deferred Charges	100,000	Surplus:		
		Balance 1/1/1911	$300,000	
		*Profits Since	800,000	
			1,100,000	
		Dividends declared in 1911	900,000	200,000
	$1,100,000			$1,100,000

* The amount of $800,000 is made up thus:

Profits	1911	$600,000
[1]Loss	1912	100,000
Profits	1913	300,000

[1] For the purpose of solving the problem assume that $50,000 of this loss was incurred in the six months ending June 30, 1912.

Prepare: (A) Consolidated working papers.
(B) Consolidated balance sheet.

Problem 6.—The following is a balance sheet of the Brown Company as at December 31, 1917:

Real Estate, Buildings and Machinery		$200,000
Patents and Goodwill		350,000
Investment in Black Company—1,800 Shares of $100 each, purchased March 31, 1917, for		270,000
Inventory	$410,000	
Bills and Accounts Receivable	320,000	
Cash	70,000	
Advances to Black Company	130,000	930,000
Total		$1,750,000
Capital Stock		$500,000
Bills Payable	405,000	
Accounts Payable	375,000	780,000
Surplus—January 1, 1917	275,000	
Profits for Year	320,000	
	595,000	
Less Dividends Paid	125,000	470,000
Total		$1,750,000

The Balance Sheet of the Black Company as at December 31, 1917, shows the following condition:

Machinery and Equipment		$460,000
Inventory	$130,000	
Accounts and Bills Receivable	80,000	
Cash	2,000	212,000
Total		$672,000
Capital Stock 2,000 Shares		$200,000
Bills Payable	$205,000	
Advances from Brown Company	130,000	
Accounts Payable	62,000	397,000
Surplus—January 1, 1917	15,000	
Profits (earned proportionately throughout the year)	60,000	75,000
Total		$672,000

Prepare a consolidated balance sheet as at December 31, 1917.

What position would you take should the client request a certified balance sheet of the Brown Company by itself as at December 31, 1917? Submit your answer in the form of a letter addressed to the client, giving reasons for your conclusions.

Problem 7.—On January 1, 1913, the A B Company acquired 90 per cent of the stock of the X Y Company and 80 per cent of the stock of the P Q Company, two subsidiary companies which it thus controlled and whose policy and general administration it directed, the minority holdings in each case being in the hands of the officers and employees of the subsidiary companies or of other interests friendly to the A B Company. On June 30, 1913, the holdings in the X Y Company were reduced to 80 per cent by the sale of 100 shares at $200 per share to certain employees not heretofore stockholders; while in the case of the P Q Company, owing to the resignation of an officer, his holdings, consisting of 100 shares, were purchased at par, the holdings by the A B Company being thus increased to 90 per cent, so that on December 31, 1913, the proportion of holdings in the two companies was just reversed.

The following are the trial balances of all three companies (after closing) at December 31, 1913:

TRIAL BALANCES at December 31, 1913

Particulars	*A B Company*		*X Y Company*		*P Q Company*	
Properties			$85,000		$75,000	
Goodwill	$100,000					
Stockholdings:						
In X Y Co., 800 shares. (book value)	115,000*					
In P Q Co., 900 shares (at cost)	82,000					
Current Assets	132,000		135,000		90,000	
Capital Stock:						
A B Co., 3,000 shares.		$300,000				
X Y Co., 1,000 shares.				$100,000		
P Q Co., 1,000 shares.						$100,000
Accounts Payable		125,000		30,000		10,000
Surplus at January 1		50,000		60,000		10,000
1913 Profits		44,000**		45,000		35,000
Dividends paid in December, 1913	30,000		40,000		25,000	
Current Accounts	60,000			25,000		35,000
	$519,000	$519,000	$260,000	$260,000	$190,000	$190,000

* After crediting the proceeds of the 100 shares sold, prior to which the investment had been valued at cost.

** Dividends received from subsidiary companies, less expenses of parent company.

Prepare a consolidated balance sheet. Assume that the profits earned by the X Y Company and the P Q Company, respectively, to June 30, 1913, were exactly 50 per cent of the profits for the complete year.

Problem 8.—From the following trial balances, after closing, prepare a consolidated balance sheet as at January 31, 1915. This consolidated balance sheet must be prepared in form suitable for submission to a firm of commercial paper brokers and to bankers.

It is assumed that you audited all these balance sheets and had every opportunity of inquiring and satisfying yourself relative to their accuracy. This being so, append to the balance sheet such a certificate as you would feel warranted in signing.

A B C MANUFACTURING COMPANY

TRIAL BALANCE—after closing—as at January 31, 1915

		Dr.	Cr.
Real Estate, Buildings, Machinery, etc.		$1,000,000	
Goodwill		1,000,000	
Investment in and advances to Paris Manufacturing Company:			
Capital Stock—at cost	$250,000		
Advances	150,000	400,000	
Accounts Receivable, less Reserve $10,000		150,000	
Inventories of Raw Material, Work in Process, Finished Material, etc.		300,000	
Cash		50,000	
Notes Payable			$250,000
Accounts Payable			50,000
Investment in and advances to Brown-Smith Company:			
Capital Stock—par value	100,000		
Advances	100,000	200,000	
First Mortgage 6% Gold Bonds			500,000
Preferred Stock—7% Cumulative—10,000 shares			1,000,000
Common Stock—10,000 shares			1,000,000
Surplus			300,000
		$3,100,000	$3,100,000

PARIS MANUFACTURING COMPANY

TRIAL BALANCE—after closing—as at January 31, 1915

	Dr.	Cr.
Real Estate, Buildings, Machinery, etc.	$250,000	
Goodwill	200,000	
Accounts Receivable	60,000	
Inventories of Raw Material, Work in Process, Finished Material, etc.	175,000	
Cash	25,000	
Reserve for Bad Debts		$10,000
Notes Payable		90,000
Accounts Payable		10,000
A B C Manufacturing Company		150,000
Capital Stock—1,500 Shares		150,000
Surplus		300,000
	$710,000	$710,000

BROWN-SMITH COMPANY

TRIAL BALANCE—after closing—as at January 31, 1915

	Dr.	Cr.
Real Estate, Buildings, Machinery, etc.	$50,000	
Accounts Receivable	25,000	
Finished Goods on Consignment—at Selling Price	100,000	
Inventories of Raw Material, Work in Process, Finished Materials, etc.	125,000	
Cash	25,000	
Notes Payable		$150,000
Accounts Payable		25,000
A B C Manufacturing Company		100,000
Capital Stock—1,000 shares		100,000
Deficit	50,000	
	$375,000	$375,000

In preparing the balance sheet required, bear the following facts in mind:

1. The dividends on the preferred stock of the A B C Manufacturing Company were paid to March 31, 1914.
2. The finished goods on consignment (Brown-Smith Balance Sheet) cost to manufacture $60,000. On realization it is estimated a profit of $10,000 will be made. Disregard any freight expense.
3. All inventories are priced on proper basis.
4. All accounts receivable are considered collectible after allowing for reserves.

Problem 9.—From the following three trial balances prepare a consolidated balance sheet as at December 31, 1912, in the form you would draw it up for presentation to the stockholders of the parent company (The Safety Razor Company) showing as separate items therein (*a*) the total goodwill of the combined companies; and (*b*) the net profits accruing to the Safety Razor Company.

SAFETY RAZOR COMPANY

TRIAL BALANCE

December 31, 1912

Preferred Stock		$1,500,000
Common Stock		1,500,000
Investments in Subsidiary Companies: 4,000 shares of stock of L W Co., and 4,000 shares of stock of Steel Blade Co., both of $100 each—at cost	$2,500,000	
Accounts Payable		20,000
Dividends from Subsidiary Companies		100,000
Administration Expenses	25,000	
L W Co., Current Account	100,000	
Steel Blade Company Advances	150,000	
Cash	270,000	
Organization Expenses	75,000	
	$3,120,000	$3,120,000

L W COMPANY

TRIAL BALANCE

December 31, 1912

Properties and Plant	$325,000	
Goodwill	250,000	
Investment in Steel Blade Co.: 2,000 shares of a par value of $100 each cost $300,000	400,000	
Inventories	250,000	
Receivables	195,000	
Cash	90,000	
Capital Stock—4,000 shares		$400,000
Accounts Payable		125,000
Steel Blade Company		175,000
Surplus (Includes $100,000 added to book value of Investment in Steel Blade Co.)		710,000
Safety Razor Company		100,000
	$1,510,000	$1,510,000

STEEL BLADE COMPANY

TRIAL BALANCE

December 31, 1912

Goodwill	$50,000	
Property and Plant	325,000	
Inventories	190,000	
Receivables—General	105,000	
L W Company	195,000	
Cash	10,000	
Capital Stock (6,000 shares)		$600,000
Accounts Payable		90,000
Safety Razor Company		150,000
Surplus		35,000
	$875,000	$875,000

In the preparation of your consolidated balance sheet, be guided by the following assumed facts:

1. That the Safety Razor Company was formed on March 28, 1912, and acquired its stock ownership in the two subsidiary companies, as shown in its trial balance on April 1, 1912.
2. That at January 1, 1912, the L W Company had a surplus of $605,000 and the Steel Blade Company a deficit of $50,000.
3. That no inventory was taken of either the L W Company or the Steel Blade between January 1 and December 31, 1912, the business of the companies being continued without interruption notwithstanding the change in ownership of the capital stocks as indicated above. It is estimated on reliable authority, which may be accepted as final, that from January 1 to March 31, 1912, the net profits of the L W Company amounted to $30,000, while during the same period the Steel Blade Company lost $15,000.
4. That prior to December 31, 1912, the L W Company declared a dividend of $100,000 payable to the parent company which was duly taken up on the books of both companies, being passed through the current accounts and charged against the surplus of the L W Company prior to December 31, 1912.
5. That the difference in the current accounts between the Steel Blade Company and the L W Company represents, as to $10,000 merchandise in transit and as to the remaining $10,000, a charge for rental of warehouse for the last six months of 1912, which has been credited to the rent account on the books of the Steel Blade Company.

Problem 10.—The Jones Investment Company on June 30, 1915, obtained a controlling interest in three operating companies, viz., A Company, B Company and C Company.

The balance sheets of the four companies as at June 30, 1916, are as follows:

Debits	*Jones Investment Co.*	*A Co.*	*B Co.*	*C Co.*
Investments in other companies:				
A Co.—60% interest (Cost $900,000)	$1,000,000			
B Co.—75% interest at cost	600,000			
C Co.—80% interest at cost	400,000			
Advances to A Co	100,000			
Advances to C Co	50,000			
Cash	50,000	$100,000	$10,000	$50,000
Accounts Receivable		100,000	50,000	100,000
Inventories		200,000	100,000	50,000
Plant		1,000,000	600,000	400,000
Deficit			40,000	
	$2,200,000	$1,400,000	$800,000	$600,000
Credits				
Capital Stock	$2,000,000	$1,000,000	$800,000	$400,000
Jones Investment Co		100,000		50,000
Surplus	200,000	300,000		150,000
	$2,200,000	$1,400,000	$800,000	$600,000
The Surplus and Deficit accounts as shown above may be analyzed as follows:				
Balance to June 30, 1915	$100,000	$200,000	$4,000	$100,000
Surplus income:				
6 months to Dec. 31, 1915		180,000	46,000	25,000
6 months to June 30, 1916	217,500	220,000	40,000*	25,000
Increase in value of A Co. stock	100,000			
Dividends paid Jan., 1916	217,500*	300,000*	50,000*	
Balance June 30, 1916	$200,000	$300,000	$40,000*	$150,000

* Indicates debit.

Prepare a consolidated balance sheet of the four companies as at June 30, 1916.

A statement of the consolidated earnings and surplus account for the year to June 30, 1916, is not required, but may be submitted if desired.

In preparing the balance sheet the following additional facts should be considered:

1. The holding company has no other source of income than the dividends from the subsidiaries, which have been taken on to its books when received.

2. In accordance with a resolution of the Board of Directors of the Jones Investment Company, the following entry was made on the holding company books at June 30, 1916.

Dr. Investment in A Co	$100,000
Cr. Surplus	100,000

3. The inventories of the A Company include $100,000 of stock purchased from B Company in 1916. The cost of these goods to the B Company was $90,000.

4. Part of the plant of the C Company was built by the A Company in September and October, 1915, at a cost of $80,000. For this work the A Company charged the C Company $95,000.

5. In February, 1916, part of the equipment of the B Company, which was carried on the books at the cost price of $50,000, was destroyed by fire. The only entry that has been made in respect to this loss was to credit the plant account with the salvage of $5,000.

Problem 11.—Following are the trial balances of Company A and its subsidiaries at December 31, 1920:

Debits	*Co. A*	*Co. B*	*Co. C*
Cash	$ 75,000	$ 50,000	$ 60,000
Accounts Receivable	350,000	190,000	420,000
Notes Receivable	200,000	60,000	40,000
Inventory, Raw Material, Jan. 1, 1920	150,000	105,000	160,000
Purchases, Raw Materials	650,000	400,000	510,000
Labor	450,000	320,000	370,000
Manufacturing Expenses	190,000	190,000	205,000
Selling Expenses	85,000	40,000	75,000
Administrative Expenses	45,000	25,000	35,000
Inventory, Goods in Process, Jan. 1, 1920	80,000	70,000	75,000
Inventory, Finished Goods, Jan. 1, 1920	90,000	65,000	80,000
Plant and Equipment	900,000	400,000	750,000
Investment in Stock of Company B	875,000		
Investment in Stock of Company C	1,200,000		
	$5,340,000	$1,915,000	$2,780,000
Credits			
Capital Stock	$3,000,000	$500,000	$800,000
Notes Payable	110,000	80,000	60,000
Accounts Payable	100,000	65,000	250,000
Bonds Payable	500,000		
Premium on Bonds	5,000		
Reserve for Depreciation	100,000	60,000	112,500
Sales	1,400,000	1,050,000	1,250,000
Surplus	125,000	160,000	307,500
	$5,340,000	$1,915,000	$2,780,000

The inventories at December 31, 1920, were:

	Co. A	*Co. B*	*Co. C*
Raw Material	$280,000	$175,000	$210,000
Goods in Process	95,000	80,000	85,000
Finished Goods	135,000	145,000	105,000

Company A purchased the entire stock issues of Companies B and C at January 1, 1920, at the prices shown in the trial balance. During the year each of the three companies declared and paid a five per cent dividend. Company A took up its dividends from Companies B and C by credits to surplus. The various entries for the dividends were the only entries affecting the surplus accounts during the year.

At December 31, 1919, Company A's inventory of raw material included goods purchased from Company B at a price of $60,000, the cost thereof to Company B being $40,000.

At the same date Company B's inventory of raw material included goods purchased from Company C for $75,000, on which Company C made a profit of $25,000.

During 1920, Company C sold goods to Company B at a price of $200,000. These goods cost Company C $160,000. Company B still owes $30,000 on these purchases, the indebtedness being included in the accounts payable.

During 1920, Company B sold goods to Company A at a cost of $300,000, and at a selling price of $375,000. Company A made cash advances totaling $400,000 to Company B during the year. The sales just mentioned were charged against the advances account, the $25,000 balance of which is included in Company B's accounts payable.

The inventories at December 31, 1920, include inter-company profits as follows:

	Raw Material	*Goods in Process*	*Finished Goods*
Company A	$20,000	$5,000	$4,000
Company B	30,000	6,000	5,000

Company A's bonds were issued July 1, 1920. They bear 5 per cent interest, payable semi-annually, and mature in five years. No interest has been paid.

Allow depreciation at five per cent per annum on the cost of the fixed assets.

Prepare the following consolidated statements: cost of goods manufactured and sold; profit and loss; surplus; balance sheet.

APPENDIX B

SOLUTIONS TO REVIEW EXERCISES FOLLOWING CHAPTER IX

(* Indicates deduction)

Case A

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$110,000			
Eliminate present book value:				
Capital stock: 90% of $100,000			$90,000	
Surplus: 90% of 20,000			18,000	
Goodwill				$2,000G
Sundry Net Assets	105,000	$120,000		225,000
	$215,000	$120,000	$108,000	$227,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A	15,000			15,000S
Co. B		20,000		
Eliminate holding company's 90%			18,000	
Minority interest 10%				2,000M
	$215,000	$120,000	$108,000	$227,000

Goodwill $2,000; minority interest $12,000; surplus $15,000.

Case B

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$119,000			
Eliminate present book value:				
Capital stock: 90% of $100,000			$90,000	
Surplus: 90% of 30,000			27,000	
Goodwill				$2,000G
Sundry Net Assets	105,000	$130,000		235,000
	$224,000	$130,000	$117,000	$237,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A	24,000			24,000S
Co. B		30,000		
Eliminate holding company's 90%			27,000	
Minority interest 10%				3,000M
	$224,000	$130,000	$117,000	$237,000

Goodwill $2,000; minority interest $13,000; surplus $24,000.

Case C

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B.*
Investment in Stock of Co. B (90%)...	$105,500			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 15,000..			13,500	
Goodwill.....				$2,000G
Sundry Net Assets.....	105,000	$115,000		220,000
	$210,500	$115,000	$103,500	$222,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A.....	10,500			10,500S
Co. B.....		15,000		
Eliminate holding company's 90%			13,500	
Minority interest 10%				1,500M
	$210,500	$115,000	$103,500	$222,000

Goodwill $2,000; minority interest $11,500; surplus $10,500.

Case D

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$83,000			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 10,000*.			9,000*	
Goodwill.....				$2,000G
Deficit:				
Co. A.....	12,000			12,000S
Co. B.....		$10,000		
Eliminate holding company's 90%			9,000	
Minority interest 10%				1,000M
Sundry Net Assets.....	105,000	90,000		195,000
	$200,000	$100,000	$90,000	$210,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
	$200,000	$100,000	$90,000	$210,000

Goodwill $2,000; minority interest $9,000; deficit $12,000.

Case AA

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B(90%) Cost	$110,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Goodwill.....				$2,000G
Sundry Net Assets.....	105,000	$120,000		225,000
	$215,000	$120,000	$108,000	$227,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A.....	15,000			15,000S
Co. B.....		20,000		
Minority: 10% of $20,000 present surplus.....				2,000M
Elim. H. C.: 90% of 20,000 surplus at acquis....			18,000	
	$215,000	$120,000	$108,000	$227,000

Goodwill $2,000; minority interest $12,000; surplus $15,000.

Case BB

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$110,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Goodwill.....				$2,000G
Sundry Net Assets.....	105,000	$130,000		235,000
	$215,000	$130,000	$108,000	$237,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A.....	15,000			15,000S
Co. B.....		30,000		
Minority: 10% of $30,000 present surplus				3,000M
Elim. H. C.: 90% of 20,000 surplus at acquis.			18,000	
Surplus: 90% of 10,000 increase				9,000S
	$215,000	$130,000	$108,000	$237,000

Goodwill $2,000; minority interest $13,000; surplus $24,000.

Case CC

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$110,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Goodwill				$2,000G
Sundry Net Assets	105,000	$115,000		220,000
	$215,000	$115,000	$108,000	$222,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A	15,000			15,000S
Co. B		15,000		
Minority: 10% of $15,000 present surplus				1,500M
Elim. H. C.: 90% of 20,000 surplus at acquis			18,000	
Surplus: 90% of 5,000 decrease				4,500*S
	$215,000	$115,000	$108,000	$222,000

Goodwill $2,000; minority interest $11,500; surplus $10,500.

Case DD

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$110,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Goodwill				$2,000G
Sundry Net Assets	105,000	$90,000		195,000
Deficit—Co. B		10,000		
Minority: 10% of $10,000* present deficit				1,000M
Elim. H. C.: 90% of 20,000 surplus at acquis.			18,000*	
Surplus: 90% of 30,000 decrease				27,000S
	$215,000	$100,000	$90,000	$225,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. A	15,000			15,000S
	$215,000	$100,000	$90,000	$225,000

Goodwill $2,000; minority interest $10,000 − $1,000 = $9,000; surplus $15,000 − $27,000 = $12,000 deficit.

Case E

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$115,000			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Goodwill				$7,000G
Sundry Net Assets	100,000	$120,000		220,000
	$215,000	$120,000	$108,000	$227,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A	15,000			15,000S
Co. B		20,000		
Eliminate holding company's 90%			18,000	
Minority interest 10%				2,000M
	$215,000	$120,000	$108,000	$227,000

Goodwill $7,000; minority interest $12,000; surplus $15,000.

Case F

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$133,000			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 40,000..			36,000	
Goodwill				$7,000G
Sundry Net Assets	100,000	$140,000		240,000
	$233,000	$140,000	$126,000	$247,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A	33,000			33,000S
Co. B		40,000		
Eliminate holding company's 90%			36,000	
Minority interest 10%				4,000M
	$233,000	$140,000	$126,000	$247,000

Goodwill $7,000; minority interest $14,000; surplus $33,000.

Case G

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$107,800			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 12,000..			10,800	
Goodwill.....				$7,000G
Sundry Net Assets.....	100,000	$112,000		212,000
	$207,800	$112,000	$100,800	$219,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A.....	7,800			7,800S
Co. B.....		12,000		
Eliminate holding company's 90%			10,800	
Minority interest 10%				1,200M
	$207,800	$112,000	$100,800	$219,000

Goodwill $7,000; minority interest $11,200; surplus $7,800.

Case H

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$89,800			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 8,000..			7,200*	
Goodwill.....				$7,000G
Sundry Net Assets.....	100,000	$92,000		192,000
Deficit:				
Co. A.....	10,200			10,200S
Co. B.....		8,000		
Eliminate holding company's 90%			7,200	
Minority interest 10%				800M
	$200,000	$100,000	$90,000	$210,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
	$200,000	$100,000	$90,000	$210,000

Goodwill $7,000; minority interest $9,200; deficit $10,200.

Case EE

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$115,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Goodwill.....				$7,000G
Sundry Net Assets.....	100,000	$120,000		220,000
	$215,000	$120,000	$108,000	$227,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A.....	15,000			15,000S
Co. B.....		20,000		
Minority: 10% of $20,000 present surplus.....				2,000M
Elim. H. C.: 90% of 20,000 surplus at acquis.....			18,000	
	$215,000	$120,000	$108,000	$227,000

Goodwill $7,000; minority interest $12,000; surplus $15,000.

Case FF

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$115,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Goodwill.....				$7,000 G
Sundry Net Assets.....	100,000	$140,000		240,000
	$215,000	$140,000	$108,000	$247,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A.....	15,000			15,000S
Co. B.....		40,000		
Minority: 10% of $40,000 present surplus				4,000M
Elim. H. C.: 90% of 20,000 surplus at acquis.			18,000	
Surplus: 90% of 20,000 increase.....				18,000S
	$215,000	$140,000	$108,000	$247,000

Goodwill $7,000; minority interest $14,000; surplus $15,000 + $18,000 = $33,000.

Case GG

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$115,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Goodwill				$7,000G
Sundry Net Assets	100,000	$112,000		212,000
	$215,000	$112,000	$108,000	$219,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A	15,000			15,000S
Co. B		12,000		
Minority: 10% of $12,000 present surplus				1,200M
Elim. H. C.: 90% of 20,000 surplus at acquis.			18,000	
Surplus: 90% of 8,000 decrease				7,200*S
	$215,000	$112,000	$108,000	$219,000

Goodwill $7,000; minority interest $11,200; surplus $15,000 − $7,200 = $7,800.

Case HH

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$115,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Goodwill				$7,000G
Sundry Net Assets	100,000	$92,000		192,000
Deficit—Co. B		8,000		
Minority: 10% of $8,000 present deficit				800M
Elim. H. C.: 90% of 20,000 surplus at acquis.			18,000*	
Surplus: 90% of 28,000 decrease				25,200S
	$215,000	$100,000	$90,000	$225,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. A	15,000			15,000S
	$215,000	$100,000	$90,000	$225,000

Goodwill $7,000; minority interest $9,200; surplus $15,000 − $25,200 = $10,200 deficit.

Case I

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$105,000			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Deduction from goodwill				$3,000*G
Sundry Net Assets	80,000	$120,000		200,000
Deficit—Co. A	15,000			15,000S
	$200,000	$120,000	$108,000	$212,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. B		20,000		
Eliminate holding company's 90%			18,000	
Minority interest 10%				2,000M
	$200,000	$120,000	$108,000	$212,000

Deduction from goodwill $3,000; minority interest $12,000; deficit $15,000.

Case J

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$123,000			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 40,000..			36,000	
Deduction from goodwill				$3,000*G
Sundry Net Assets	80,000	$140,000		220,000
	$203,000	$140,000	$126,000	$217,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A	3,000			3,000S
Co. B		40,000		
Eliminate holding company's 90%			36,000	
Minority interest 10%				4,000M
	$203,000	$140,000	$126,000	$217,000

Deduction from goodwill $3,000; minority interest $14,000; surplus $3,000.

Case K

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S* .
Investment in Stock of Co. B (90%)...	$97,800			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 12,000..			10,800	
Deduction from goodwill.....				$3,000*G
Sundry Net Assets.....	80,000	$112,000		192,000
Deficit—Co. A.....	22,200			22,200S
	$200,000	$112,000	$100,800	$211,200
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. B.....		12,000		
Eliminate holding company's 90%			10,800	
Minority interest 10%				1,200M
	$200,000	$112,000	$100,800	$211,200

Deduction from goodwill $3,000; minority interest $11,200; deficit $22,200.

Case L

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$79,800			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 8,000..			7,200*	
Deduction from goodwill.....				$3,000*G
Sundry Net Assets.....	80,000	$92,000		172,000
Deficit:				
Co. A.....	40,200			40,200 S
Co. B.....		8,000		
Eliminate holding company's 90%			7,200	
Minority interest 10%				800M
	$200,000	$100,000	$90,000	$210,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
	200,000	100,000	90,000	210,000

Deduction from goodwill $3,000; minority interest $9,200; deficit $40,200.

Case II

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$105,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Deduction from goodwill.....				$3,000*G
Sundry Net Assets.....	80,000	$120,000		200,000
Deficit—Co. A.....	15,000			15,000S
	$200,000	$120,000	$108,000	$212,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. B.....		20,000		
Minority: 10% of $20,000 present surplus				2,000M
Elim. H. C.: 90% of 20,000 surplus at acquis.			18,000	
	$200,000	$120,000	$108,000	$212,000

Deduction from goodwill $3,000; minority interest $12,000; deficit $15,000.

Case JJ

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$105,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Deduction from goodwill.....				$3,000*G
Sundry Net Assets.....	80,000	$140,000		220,000
Deficit—Co. A.....	15,000			15,000S
	$200,000	$140,000	$108,000	$232,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. B.....		40,000		
Minority: 10% of $40,000 present surplus				4,000M
Elim. H. C.: 90% of 20,000 surplus at acquis.			18,000	
Surplus: 90% of 20,000 increase				18,000S
	$200,000	$140,000	$108,000	$232,000

Deduction from goodwill $3,000; minority interest $14,000; surplus $18,000—$15,000, or $3,000.

Case KK

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$105,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Deduction from goodwill.....				$3,000*G
Sundry Net Assets.....	80,000	$112,000		192,000
Deficit—Co. A.....	15,000			15,000S
	$200,000	$112,000	$108,000	$204,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. B.....		12,000		
Minority: 10% of $12,000 present surplus				1,200M
Elim.H.C.: 90% of 20,000 surplus at acquis.			18,000	
Surplus: 90% of 8,000 decrease				7,200*S
	$200,000	$112,000	$108,000	$204,000

Deduction from goodwill $3,000; minority interest $11,200; deficit $15,000 $7,200 = $22,200.

Case LL

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$105,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 20,000..			18,000	
Deduction from goodwill.....				$3,000*G
Sundry Net Assets.....	80,000	$92,000		172,000
Deficit:				
Co. A.....	15,000			15,000S
Co. B.....		8,000		
Minority: 10% of $8,000 present deficit				800M
Elim. H. C.: 90% of 20,000 surplus at acquis.			18,000*	
Surplus: 90% of 28,000 decrease				25,200 S
	$200,000	$100,000	$90,000	$210,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
	$200,000	$100,000	$90,000	$210,000

Deduction from goodwill $3,000; minority interest $9,200; deficit $40,200.

Case M

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$85,000			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 10,000..			9,000*	
Goodwill.....				$4,000G
Sundry Net Assets.....	130,000	$90,000		220,000
Deficit—Co. B.....		10,000		
Eliminate holding company's 90%			9,000	
Minority interest 10%				1,000M
	$215,000	$100,000	$90,000	$225,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. A.....	15,000			15,000 S
	$215,000	$100,000	$90,000	$225,000

Goodwill $4,000; minority interest $9,000; surplus $15,000.

Case N

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$92,200			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 2,000..			1,800*	
Goodwill.....				$4,000G
Sundry Net Assets.....	130,000	$98,000		228,000
Deficit—Co. B.....		2,000		
Eliminate holding company's 90%			1,800	
Minority interest 10%				200M
	$222,200	$100,000	$90,000	$232,200
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. A.....	22,200			22,200S
	$222,200	$100,000	$90,000	$232,200

Goodwill $4,000; minority interest $9,800; surplus $22,200.

Case O

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$104,800			
Eliminate present book value:				
Capital stock: 90% of $100,000			$90,000	
Surplus: 90% of 12,000			10,800	
Goodwill				$4,000G
Sundry Net Assets	130,000	$112,000		242,000
	$234,800	$112,000	$100,800	$246,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A	34,800			34,800S
Co. B		12,000		
Eliminate holding company's 90%			10,800	
Minority interest 10%				1,200M
	$234,800	$112,000	$100,800	$246,000

Goodwill $4,000; minority interest $11,200; surplus $34,800.

Case P

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)	$77,800			
Eliminate present book value:				
Capital stock: 90% of $100,000			$90,000	
Deficit: 90% of 18,000			16,200*	
Goodwill				$4,000G
Sundry Net Assets	130,000	$82,000		212,000
Deficit—Co. B		18,000		
Eliminate holding company's 90%			16,200	
Minority interest 10%				1,800M
	$207,800	$100,000	$90,000	$217,800
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. A	7,800			7,800
	$207,800	$100,000	$90,000	$217,800

Goodwill $4,000; minority interest $8,200; surplus $7,800.

Case MM

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$85,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000			$90,000	
Deficit: 90% of 10,000			9,000*	
Goodwill				$4,000G
Sundry Net Assets	130,000	$90,000		220,000
Deficit—Co. B		10,000		
Eliminate holding company's 90%			9,000	
Minority interest 10%				1,000M
	$215,000	$100,000	$90,000	$225,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. A	15,000			15,000S
	$215,000	$100,000	$90,000	$225,000

Goodwill $4,000; minority interest $9,000; surplus $15,000.

Case NN

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$85,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000			$90,000	
Deficit: 90% of 10,000			9,000*	
Goodwill				$4,000G
Sundry Net Assets	130,000	$98,000		228,000
Deficit—Co. B		2,000		
Minority: 10% of $2,000 present deficit				200M
Elim. H. C. 90% of 10,000 deficit at acquis.			9,000	
Surplus: 90% of 8,000 gain since acquis.				7,200*S
	$215,000	$100,000	$90,000	$225,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. A	15,000			15,000S
	$215,000	$100,000	$90,000	$225,000

Goodwill $4,000; minority interest $9,800; surplus $15,000 + $7,200 = $22,200.

Case OO

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$85,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 10,000..			9,000*	
Goodwill				$4,000G
Sundry Net Assets	130,000	$112,000		242,000
	$215,000	$112,000	$81,000	$246,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A	15,000			15,000S
Co. B		12,000		
Minority: 10% of $12,000 present surplus				1,200M
Elim. H. C. 90% of 10,000 deficit at acquis.			9,000*	
Surplus 90% of 22,000 gain				19,800S
	$215,000	$112,000	$81,000	$246,000

Goodwill $4,000; minority interest $11,200; surplus $15,000 + $19,800 = $34,800

Case PP

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$85,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 10,000..			9,000*	
Goodwill				$4,000G
Sundry Net Assets	130,000	$82,000		212,000
Deficit—Co. B		18,000		
Minority: 10% of $18,000 present deficit				1,800M
Elim. H. C. 90% of 10,000 deficit at acquis.			9,000	
Surplus 90% of 8,000 loss.				7,200S
	$215,000	$100,000	$90,000	$225,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. A	15,000			15,000S
	$215,000	$100,000	$90,000	$225,000

Goodwill $4,000; minority interest $8,200; surplus $15,000 — $7,200 = $7,800.

Case Q

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$80.000			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 10,000..			9,000*	
Deduction from goodwill				$1,000*G
Sundry Net Assets	105,000	$90,000		195,000
Deficit				
Co. A	15,000			15,000S
Co. B		10,000		
Eliminate holding company's 90%			9,000	
Minority interest 10%				1,000M
	$200,000	$100,000	$90,000	$210,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
	$200,000	$100,000	$90,000	$210,000

Deduction from goodwill $1,000; minority interest $9,000; deficit $15,000.

Case R

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$87,200			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 2,000..			1,800*	
Deduction from goodwill				$1,000*G
Sundry Net Assets	105,000	$98,000		203,000
Deficit:				
Co. A	7,800			7,800S
Co. B		2,000		
Eliminate holding company's 90%			1,800	
Minority interest 10%				200M
	$200,000	$100,000	$90,000	$210,000
Liabilities				
Capital Stock:				
Co. A	$200,000			$200,000
Co. B		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
	$200,000	$100,000	$90,000	$210,000

Deduction from goodwill $1,000; minority interest $9,800; deficit $7,800.

Case S

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$99,800			
Eliminate present book value:				
Capital stock: 90% of $100,000..			$90,000	
Surplus: 90% of 12,000..			10,800	
Deduction from goodwill.....				$1,000*G
Sundry Net Assets.....	105,000	$112,000		217,000
	$204,800	$112,000	$100,800	$216,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus:				
Co. A.....	4,800			4,800S
Co. B.....		12,000		
Eliminate holding company's 90%			10,800	
Minority interest 10%				1,200M
	$204,800	$112,000	$100,800	$216,000

Deduction from goodwill $1,000; minority interest $11,200; surplus $4,800.

Case T

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%)...	$72,800			
Eliminate present book value:				
Capital stock: 90% of 100,000..			$90,000	
Deficit: 90% of 18,000..			16,200*	
Deduction from goodwill.....				$1,000*G
Sundry Net Assets.....	105,000	$82,000		187,000
Deficit:				
Co. A.....	22,200			22,200S
Co. B.....		18,000		
Eliminate holding company's 90%			16,200	
Minority interest 10%				1,800 M
	$200,000	$100,000	$90,000	$210,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
	$200,000	$100,000	$90,000	$210,000

Deduction from goodwill $1,000; minority interest $8,200; deficit $22,200.

Case QQ

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$80,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 10,000..			9,000*	
Deduction from goodwill.....				$1,000*G
Sundry Net Assets.....	105,000	$90,000		195,000
Deficit:				
Co. A.....	15,000			15,000S
Co. B.....		10,000		
Minority 10% of $10,000 present deficit.....				1,000 M
Elim. H. C. 90% of 10,000 deficit at acquis.....			9,000	
	$200,000	$100,000	$90,000	$210,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				$10,000M
	$200,000	$100,000	$90,000	$210,000

Deduction from goodwill $1,000; minority interest $9,000; deficit $15,000.

Case RR

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$80,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 10,000..			9,000*	
Deduction from goodwill.....				$1,000*G
Sundry Net Assets.....	105,000	$98,000		203,000
Deficit:				
Co. A.....	15,000			15,000S
Co. B.....		2,000		
Minority: 10% of $2,000 present deficit				200 M
Elim. H. C. 90% of 10,000 deficit at acquis.			9,000	
Surplus 90% of 8,000 gain				7,200 *S
	$200,000	$100,000	$90,000	$210,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
	$200,000	$100,000	$90,000	$210,000

Deduction from goodwill $1,000; minority interest $9,800; deficit $15,000 − $7,200 = $7,800.

Case SS

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$80,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 10,000..			9,000*	
Deduction from goodwill.....				$1,000*G
Sundry Net Assets.....	105,000	$112,000		217,000
Deficit—Co. A.....	15,000			15,000S
	$200,000	$112,000	$81,000	$231,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
Surplus—Co. B.....		12,000		
Minority: 10% of $12,000 present surplus				1,200M
Elim. H. C. 90% of 10,000 deficit at acquis. ———			9,000*	
Surplus 90% of 22,000 gain				19,800
	$200,000	$112,000	$81,000	$231,000

Deduction from goodwill $1,000; minority interest $11,200; surplus $19,800 − $15,000 = $4,800.

Case TT

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (90%) Cost	$80,000			
Eliminate book value at acquisition:				
Capital stock: 90% of $100,000..			$90,000	
Deficit: 90% of 10,000..			9,000*	
Deduction from goodwill.....				$1,000*G
Sundry Net Assets.....	105,000	$82,000		187,000
Deficit:				
Co. A.....	15,000			15,000S
Co. B.....		18,000		
Minority: 10% of $18,000 present deficit				1,800M
Elim. H. C. 90% of 10,000 deficit at acquis. ———			9,000	
Surplus 90% of 8,000 loss.				7,200S
	$200,000	$100,000	$90,000	$210,000
Liabilities				
Capital Stock:				
Co. A.....	$200,000			$200,000
Co. B.....		$100,000		
Eliminate holding company's 90%			$90,000	
Minority interest 10%				10,000M
	$200,000	$100,000	$90,000	$210,000

Deduction from goodwill $1,000; minority interest $8,200; deficit $15,000 + $7,200 = $22,200.

APPENDIX C

SOLUTIONS TO PROBLEMS IN APPENDIX A

Solution to problem 1.

JOURNAL ENTRIES ON THE BOOKS OF THE HOLDING COMPANY

February, 1905

Investment in Stock of Company A.....	$168,750.00	
Cash.....		$168,750.00
To record the purchase of three-fourths of the stock of Company A, at book value at December 31, 1904.		
Capital Stock.....	$150,000	
Surplus.....	75,000	
Total.....	$225,000	

Three-fourths thereof = $168,750.

March, 1905

Investment in Stock of Company B.....	416,666.67	
Cash.....		416,666.67
To record the purchase of two-thirds of the stock of Company B, at book value at December 31, 1904.		
Capital Stock.....	$500,000	
Surplus.....	125,000	
Total.....	$625,000	

Two-thirds thereof = $413,333.33

January, 1906

Investment in Stock of Company A.....	3,750.00	
Income from Investment in Company A.....		3,750.00
To take up our three-fourths of the net profits of Company A as shown by their profit and loss statement for the year 1905.		

January, 1906

Investment in Stock of Company B.....	33,333.33	
Income from Investment in Company B.....		33,333.33
To take up our two-thirds of the net profits of Company B as shown by their profit and loss statement for the year 1905.		

February 15, 1906

Dividends Receivable—Company A	$11,250.00	
Investment in Stock of Company A		$11,250.00
To record declaration of dividend of 10% by Company A		
Cash	11,250.00	
Dividends Receivable—Company A		11,250.00
To record receipt of dividend on stock of Company A		

NOTE.—The problem does not indicate any interval between the declaration and payment of the dividend. The above entries are given to indicate how the facts would be recorded if there had been an interval. The following single entry in the case of Company B shows how the facts may be recorded when no time intervenes between the declaration and payment of the dividend.

February 14, 1906

Cash	$26,666.67	
Investment in Stock of Company B		$26,666.67
To record reduction of investment by reason of payment by Company B of a dividend of 8%.		

These entries indicate the proper method of recording earnings of and dividends from subsidiaries, as explained in Chapter VII. The holding company should take up as income its share of the profits of the subsidiary, and not the dividends which it receives. In the case of Company A, its share of the earnings was only $3,750, although it received dividends of $11,250. $7,500 of the cash received was therefore a conversion of the investment into cash. If the entire dividend had been treated as income the earnings for the year would have been overstated, as would also the carrying value of the investment. On the other hand, Company B did not declare dividends equal to its earnings. If the holding company had taken up only its share of the dividends as income, its earnings for the year would have been understated, and the carrying value of the investment in Company B stock would also have been understated.

It will be noted that the stock of Company A was purchased in February and the stock of Company B was purchased in March. The question arises as to whether any consideration should be given to this fact in the entries for the stock purchases and the profits for the year, as well as in the preparation of the consolidated balance sheet.

The entries for the purchase would not be affected, even if it were certain that profits had accrued at the dates of purchase, for the investment accounts should be charged with the price paid regardless of the book value at the date of acquisition.

As to the entries for income determined at the end of the year, it must be remembered that the law does not consider corporate profits as accruing from day to day. Moreover, seasonal fluctuations usually make it unsafe to assume that profits are made in uniform amounts throughout the year. These facts, together with the added fact that Company C clearly paid nothing for accrued profits, justify the holding company in considering as profits its share of the year's income of the two companies.

In preparing the consolidated balance sheet, the book value at the date of the balance sheet will be eliminated from the investment account. Since the balance of the investment account is exactly equal to the book value of the stock held, there will be no goodwill element. It may be contended that the book value of the stock of each company at the date of purchase was actually in excess of the purchase price because of profits earned since the first of the year, and that there was therefore a negative goodwill item involved in the stock purchase. There are three objections to accepting this theory.

In the first place, even if the theory were accepted as sound, there is no sure way of determining just how much profit was earned up to the date of purchase and hence no way of ascertaining the amount of the negative goodwill.

In the second place, if a negative goodwill is to be arrived at in the consolidated working papers, the balance of the investment account must be less than the book value at the date of the balance sheet. To have the balance of the investment account less than book value at the end of 1906, it would be necessary to charge the investment account with only that portion of the year's profit earned by the subsidiary after the holding company acquired the stock. It has already been shown that it is proper for the holding company to take up the entire year's profit.

In the third place, assuming for the sake of argument that it would be possible to prorate the year's profits, and that it would be proper to take up only the profits earned after acquisition, the results in this case would be the same so far as the consolidated balance sheet is concerned. There are no goodwill

accounts on the books of the subsidiaries and hence the excess of book value over purchase price arising from profits between January 1 and the dates of acquisition could not be treated as negative goodwill to be offset against goodwill accounts, but would be added to the surplus on the consolidated balance sheet.

Solution to problem 2.—

X Y Z COMPANY AND SUBSIDIARY

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

January 1, 1910

Assets	*X Y Z Co.*	*P Q Co.*	*I. Co.*	*Elim.*	*C. B. S.*
Real Estate	$50,000	$25,000			$75,000
Building, Plant and Equipment	75,000	45,000			120,000
Goodwill	25,000				25,000 G
Investment in P Q Co. (100%) Cost	150,000				
Eliminate book value at acquisition:					
Capital stock			$100,000		
Surplus			25,000		
Goodwill					25,000 G
Inventories	80,000	20,000			100,000
Accounts Receivable	70,000	85,000	15,000		140,000
	$450,000	$175,000	$140,000		$485,000
Liabilities					
Accounts Payable	$50,000	$50,000	$15,000		$85,000
Loans	50,000				50,000
Capital Stock:					
X Y Z Company	250,000				250,000
P Q Company		100,000			
Eliminate holding company's 100 %			100,000		
Surplus:					
X Y Z Company	100,000				100,000S
P Q Company		25,000			
Eliminate holding company's 100% at acquisition			25,000		
	$450,000	$175,000	$140,000		$485,000

X Y Z COMPANY AND SUBSIDIARY P Q COMPANY

CONSOLIDATED BALANCE SHEET

January 1, 1910

Assets			*Liabilities*		
Fixed Assets:			Current Liabilities:		
Real Estate	$75,000		Accounts Payable	$85,000	
Building, Plant and Equipment	120,000		Loans	50,000	$135,000
Goodwill	50,000	$245,000			
Current Assets:			Capital:		
Inventories	100,000		Capital Stock	250,000	
Accounts Receivable	140,000	240,000	Surplus	100,000	350,000
		$485,000			$485,000

Solution to problem 3.—

COMPANY A AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

June 30, 1917

Assets	*Co. A*	*Co. B*	*Co. C*	*Elim.*	*C. B. S.*
Property and Goodwill	$850,000	$650,000	$1,130,000		$2,630,000
Investment in Stock of Co. B (100%) Cost	700,000				
Eliminate book value at acquisition:					
Capital stock				$400,000	
Surplus				200,000	
Goodwill					100,000
Investment in Stock of Co. C (100%) Cost	800,000				
Eliminate book value at acquisition:					
Capital stock				1,000,000	
Surplus				30,000	
Capital Surplus					230,000*S
Current Assets	700,000	60,000	180,000		940,000
	$3,050,000	$710,000	$1,310,000	$1,630,000	$3,440,000

COMPANY A AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET—WORKING PAPERS—*Continued*

June 30, 1917

Liabilities	*Co. A*	*Co. B*	*Co. C*	*Elim.*	*C. B. S.*	
Capital Stock:						
Company A	$2,250,000				$2,250,000	
Company B		$400,000				
Eliminate holding company's 100%				$400,000		
Company C			$1,000,000			
Eliminate holding company's 100%				1,000,000		
Surplus, January 1, 1917: (Date of acquisition)						
Company A	525,000				525,000	S
Company B		200,000				
Eliminate holding company's 100%				200,000		
Company C			30,000			
Eliminate holding company's 100%				30,000		
Profits to June 30	125,000	100,000	40,000		265,000	S
Current Liabilities	150,000	10,000	240,000		400,000	
	$3,050,000	$710,000	$1,310,000	$1,630,000	$3,440,000	

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED BALANCE SHEET

June 30, 1917

Assets		*Liabilities*	
Property and Goodwill	$2,730,000	Capital Stock	$2,250,000
Current Assets	940,000	Capital Surplus	230,000
		Surplus	790,000
		Current Liabilities	400,000
	$3,670,000		$3,670,000

The $230,000 excess of book value of Company C's stock over the purchase price is shown on the balance sheet as capital surplus. Company C has no goodwill account, and the value of its property at January 1, the date of acquisition, was established by appraisal; moreover, C's profits for the half year were four per cent of its capital stock, or on the basis of eight per cent per annum. It is difficult to see how this advantageous purchase lessens the value of the goodwill on the books of A or B, or the goodwill arising from A's purchase of B's stock.

Solution to problem 4.

(*A*) *Effect on Balance Sheet of Company B, the Subsidiary.*

BALANCE SHEET OF COMPANY B (before paying dividend)

Cash*	$ 25,000	Capital Stock	$100,000
Other Net Assets	125,000	Surplus	50,000
	$150,000		$150,000

* Cash assumed to be on hand because used for dividend.

BALANCE SHEET OF COMPANY B (after paying dividend)

Other Net Assets	$125,000	Capital Stock	$100,000
		Surplus	25,000
	$125,000		$125,000

The dividend causes a reduction of $25,000 in the cash and the surplus.

(*B*) *Effect on Balance Sheet of Company A, the Holding Company.*

The dividend would increase Company A's cash $24,500. If Company A treated the dividend as a reduction of the investment account, the balance would be reduced from $196,000 to $171,500. If the dividend was treated as income, the investment account would remain unchanged and the surplus would be increased $24,500. This would be misleading because it would make the dividend appear to be an earning of Company A, whereas in reality it was merely a conversion of part of its investment in the subsidiary into cash.

BALANCE SHEET OF COMPANY A (before dividend)

(*C*) *Effect on the Consolidated Balance Sheet.*

CONSOLIDATED WORKING PAPERS (before dividend)

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B	$196,000			
Eliminate book value:				
Capital stock: 98% of $100,000			$98,000	
Surplus: 98% of 50,000			49,000	
Goodwill				$49,000 G
Cash		$25,000		25,000
Other Net Assets		125,000		125,000
Liabilities				
Capital Stock		100,000		
Eliminate Co. A's 98%			98,000	
Minority 2%				2,000M
Surplus		50,000		
Eliminate Co. A's 98%			49,000	
Minority 2%				1,000M

CONSOLIDATED WORKING PAPERS (after dividend)

(On assumption that holding company credited dividend to investment)

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B	$171,500			
Eliminate present book value:				
Capital stock: 98% of $100,000			$98,000	
Surplus: 98% of 25,000			24,500	
Goodwill				$49,000
Cash	24,500			24,500
Other Net Assets		$125,000		125,000
Liabilities				
Capital Stock		100,000	98,000	2,000M
Surplus		25,000		
Elim. Co. A's 98% of $25,000 present surplus			24,500	
Minority 2% of 25,000 present surplus				500M

CONSOLIDATED WORKING PAPERS (after dividend)

(On assumption that holding company credited the dividends to surplus)

Assets	*Co. A*	*Co. B*	*Elim.*	*C. B. S.*
Investment in Stock of Co. B (98%) Cost	$196,000			
Eliminate book value at acquisition:				
Capital stock: 98% of $100,000			$98,000	
Surplus: 98% of 50,000			49,000	
Goodwill				$49,000
Cash	24,500			24,500
Other Net Assets		$125,000		125,000
Liabilities				
Capital Stock		100,000		
Eliminate holding company's 98%			98,000	
Minority 2%				2,000M
Surplus:				
Co. A	$24,500			24,500 S
Co. B		25,000		
Minority: 2% of $25,000 present surplus				500M
Elim. Co. A's 98% of 50,000 surplus at acquis			49,000	
Surplus 98% of 25,000 decrease				24,500*S

The consolidated balance sheet will be the same no matter whether the holding company credits the dividend to the investment account or to the surplus account. It will differ from the consolidated balance sheet prior to the dividend in two particulars: the cash and the minority interest will each be $500 smaller than before because of the cash paid to the outside stockholders.

Solution to problem 5.—Since the holding company is carrying its investments at cost, the eliminations will be based on the book value of the subsidiaries' stock at the dates of acquisition. Therefore it is necessary to determine the surplus of each company at the date when the holding company acquired its stock.

Company B.—The date of acquisition was January 1, 1910, and B's surplus at that date was $100,000, as shown in its balance sheet.

Company C.—(Date of acquisition—July 1, 1908.)

Deficit, January 1, 1906	$250,000
Add Profits from January 1, 1906, to July 1, 1908:	
Profits from January 1, 1906, to Dec. 31, 1913 = $650,000	
These profits are assumed to have been made in uniform amounts monthly. Then if	
$650,000 = Profits for 8 years	
81,250 = Profits for 1 year	
From January 1, 1906, to July 1, 1908, is 2½ years	
Then $81,250 x 2½ =	203,125
Deficit at July 1, 1908	$46,875

Company D.—(Date of acquisition—June 30, 1912.)

Surplus, January 1, 1911	$300,000
Add Profits for 1911	600,000
Total	900,000
Less Dividends declared in 1911	900,000
Balance at January 1, 1912	0
Loss, January 1, 1912, to June 30, 1912	50,000
Deficit, June 30, 1912	$50,000

COMPANY A AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

December 31, 1913

Assets	*Co. A*	*Co. B*	*Co. C*	*Co. D*	*Inter-Co. Eliminations*	*C. B. S.*
Investment in Stock of Co. B (75%) Cost	$1,000,000					
Eliminate book value at acquisition:						
Capital stock, 4,500 shares					$450,000.00	
Surplus—75% of $100,000					75,000.00	
Goodwill						$475,000.00 G
Investment in Stock of Co. C (70%) Cost	750,000					
Eliminate book value at acquisition:						
Capital stock, 5,600 shares					560,000.00	
Deficit—70% of $46,875					32,812.50*	
Goodwill						222,812.50 G
Investment in Stock of Co. D (80%) Cost	850,000					
Eliminate book value at acquisition:						
Capital stock, 6,400 shares					640,000.00	
Deficit—80% of $50,000					40,000.00*	
Goodwill						250,000.00 G
Other Sundry Assets	1,400,000					1,400,000.00
Fixed Assets		$500,000	$700,000	$500,000		1,700,000.00
Current Assets		500,000	250,000	500,000		1,250,000.00
Deferred Charges		100,000	50,000	100,000		250,000.00
	$4,000,000	$1,100,000	$1,000,000	$1,100,000	$1,652,187.50	$5,547,812.50

Liabilities	*Co. A*	*Co. B*	*Co. C*	*Co. D*	*Inter Co. Eliminations*	*C. B. S.*
Capital Stock:						
Company A	$2,000,000					$2,000,000.00
Company B		$600,000				
Eliminate holding company's 75%					$450,000.00	
Minority interest 25%						150,000.00M
Company C			$800,000			
Eliminate holding company's 70%					560,000.00	
Minority interest 30%						240,000.00M
Company D				$800,000		
Eliminate holding company's 80%					640,000.00	
Minority interest 20%						160,000.00M
Collateral Trust Notes 5%	1,000,000					1,000,000.00
Current Liabilities		100,000	300,000	100,000		500,000.00
Surplus:						
Company A	1,000,000					1,000,000.00 S
Company B		400,000				
Minority 25% of $400,000 Pres. Surp						100,000.00M
Elim. H. C. 75% of 100,000 Surp. at Acquisition					75,000.00	
Surplus 75% of $300,000 Increase						225,000.00 S
Company C			100,000*			
Minority 30% of $100,000 Pres. Deficit						30,000.00M*
Elim. H. C. 70% of 46,875 Def. at Acquisition					32,812.50*	
Surplus 70% of $53,125 Loss						37,187.50 S*
Company D				200,000		
Minority 20% of $200,000 Pres. Surp						40,000.00M
Elim. H. C. 80% of 50,000 Def. at Acquisition					40,000.00*	
Surplus 80% of $250,000 Gain						200,000.00 S
	$4,000,000	$1,100,000	$1,000,000	$1,100,000	$1,652,187.50	$5,547,812.50

COMPANY A AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

December 31, 1913

Assets		*Liabilities*		
Goodwill	$ 947,812.50	Capital Stock		$2,000,000.00
Other Sundry Assets	1,400,000.00	Surplus		1,387,812.50
Fixed Assets	1,700,000.00	Minority Interest:		
Current Assets	1,250,000.00	Co. B (25%)	$250,000	
Deferred Charges	250,000.00	Co. C (30%)	210,000	
		Co. D (20%)	200,000	660,000.00
		Collateral Trust 5% Notes		1,000,000.00
		Current Liabilities		500,000.00
	$5,547,812.50			$5,547,812.50

Solution to problem 6.—

THE BROWN COMPANY AND SUBSIDIARY

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

December 31, 1917

Assets	*Brown Co.*	*Black Co.*	*Inter Co. Eliminations*	*C. B. S.*
Real Estate, Buildings and Machinery	$200,000	$460,000		$660,000
Patents and Goodwill	350,000			350,000
Investment in Black Co. (1,800 shares, par 100) Cost	270,000			
Eliminate book value at acquisition:				
Capital stock			$180,000	
Surplus*: 90% of $30,000			27,000	
Goodwill				63,000 G
Inventory	410,000	130,000		540,000
Bills and Accounts Receivable	320,000	80,000		400,000
Cash	70,000	2,000		72,000
Advances to Black Company	130,000		130,000	
	$1,750,000	$672,000	$337,000	$2,085,000

* The surplus of the Black Company at March 31, 1917, the date when the Brown Company acquired the stock, was:

Surplus at January 1, 1917	$15,000
Earnings to March 31 (¼ of $60,000)	15,000
Surplus at date of acquisition	30,000

Liabilities				
Capital Stock:				
Brown Company	$500,000			$500,000
Black Company		$200,000		
Eliminate holding company's 1,800 shares			$180,000	
Minority interest				20,000M
Bills Payable	405,000	205,000		610,000
Accounts Payable	375,000	62,000		437,000
Advances from Brown Company		130,000	130,000	
Surplus:				
Brown Company	470,000			470,000 S
Black Company		75,000		
Minority: 10% of $75,000 present surplus				7,500M
Elim. H. C.'s 90% of 30,000 surplus at acquisition			27,000	
Surplus 90% of 45,000 increase since acquisition				40,500 S
	$1,750,000	$672,000	$337,000	$2,085,000

THE BROWN COMPANY AND SUBSIDIARY

CONSOLIDATED BALANCE SHEET

December 31, 1917

Assets

Fixed Assets:		
Real Estate, Buildings and Machinery	$660,000	
Patents and Goodwill	413,000	$1,073,000
Current Assets:		
Inventory	540,000	
Bills and Accounts Receivable	400,000	
Cash	72,000	1,012,000
		$2,085,000

Liabilities

Capital:		
Capital Stock	500,000	
Surplus	510,500	$1,010,500
Minority Interest:		
10% Interest in the Black Company		27,500
Current Liabilities:		
Bills Payable	610,000	
Accounts Payable	437,000	1,047,000
		$2,085,000

President ——,
The Brown Company.

DEAR SIR:

If you desire a certified balance sheet of the Brown Company alone at December 31, 1917, I should be willing to certify to such a statement after auditing your books. In fact, unless I audit the books of the BLACK COMPANY also, the only balance sheet to which I could append an unqualified certificate would be one of the BROWN COMPANY alone, showing your investment in the BLACK COMPANY at cost.

Such a balance sheet is not as desirable, however, as a consolidated balance sheet, for two reasons. In the first place, the cost of the stock, $270,000, and the advances, $130,000, represent a total investment of $400,000 in the subsidiary. You virtually own the BLACK COMPANY, and a consolidated balance sheet showing the assets and liabilities which this investment represents, with the interest of the minority stockholders therein, is a much more comprehensive and satisfactory statement of your financial condition.

In the second place, your balance sheet alone does not do you justice. Showing the investment account and the advances would raise a question in the minds of the readers of your balance sheet as to whether the net assets of the BLACK COMPANY are good enough in nature and sufficient in amount to warrant so heavy an investment and such large advances. A consolidated balance sheet taking up the BLACK COMPANY'S assets and liabilities would show clearly that the financial condition of the organization is sound and would allay any doubts. Moreover, if I were to certify to your balance sheet alone, without an audit of the books of the subsidiary to verify their profits, I could show only your own surplus of $470,000; but in a consolidated balance sheet, if the profits of the BLACK COMPANY are correctly stated, I could take up your 90% of the earnings since March 31, when you acquired the stock. This addition of $40,500 would make your surplus in the consolidated balance sheet $510,500.

Yours very truly,

Solution to problem 7.—Since the holding company is taking up its proportion of subsidiary dividends as income, it is evidently their intention to carry the investment accounts at cost, but they have confused their records so far as the X Y stock is concerned by crediting the investment account with the selling price of the 100 shares sold, so that the balance of the account no longer represents the cost of the 800 shares still held. Therefore the profit on the shares sold must be ascertained and the investment account adjusted.

Balance of X Y Co. investment account	800	shares	$115,000
Add back selling price of	100	"	20,000
Cost of	900	"	135,000
Cost per share			150
Cost of 800 shares still held			120,000
Cost of 100 shares sold			15,000

The investment account should be raised to $120,000, the cost of the 800 shares retained, and Surplus should be credited with the $5,000 profit realized by selling for $20,000 the 100 shares which cost $15,000. This is accomplished by the following entry:

Investment in X Y Co. Stock	$5,000	
Surplus		$5,000

To adjust the investment account to $120,000, the cost of 800 shares still owned, and to take up the $5,000 profit on the sale at 200 of 100 shares which cost 150.

Since the P Q Company investment account contains the cost of two purchases, it will be well to divide the balance of the account into two amounts representing the cost of the various purchases, so that the goodwill element may be measured by elimination of book values at the respective dates. The cost of the two purchases is ascertained thus:

Balance of P Q Co. investment account—cost of	900	shares	$82,000
Cost of June 30th purchase at par	100	"	10,000
Cost of first purchase	800	"	$72,000

THE A B COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

December 31, 1913

Assets	*A B Co.*	*X Y Co.*	*P Q Co.*	*I.-Co. Elim.*	*C. B. S.*
Properties		$85,000	$75,000		$160,000
Goodwill	$100,000				100,000 G
Investment in X Y Company: (800 shares) Cost	120,000				
Eliminate book value at acquisition—January 1, 1913:					
Capital stock				$80,000	
Surplus 80% of $60,000				48,000	
Deduction from goodwill					8,000*G
Investments in P Q Company: (900 shares) Cost	82,000				
First purchase—January 1, 1913—800 shares: cost $72,000					
Eliminate book value at acquisition:					
Capital stock				80,000	
Surplus 80% of $10,000				8,000	
Second purchase—June 30, 1913—100 shares: cost $10,000					
Eliminate book value at acquisition:					
Capital stock				10,000	
Surplus 10% of $27,500				2,750	
Deduction from goodwill					18,750*G
Current Assets	132,000	135,000	90,000		357,000
Current Accounts	60,000			60,000	
	$494,000	$220,000	$165,000	$288,750	$590,250

Liabilities	*A B Co.*	*X Y Co.*	*P Q Co.*	*I.-Co. Elim.*	*C. B. S.*
Capital Stock:					
A B Co	$300,000				$300,000
X Y Co		$100,000			
Eliminate holding company's 80%				$80,000	
Minority interest 20%					20,000M
P Q Co			$100,000		
Eliminate holding company's 90%				90,000	
Minority interest 10%					10,000M
Accounts Payable	125,000	30,000	10,000		165,000
Surplus:					
A B Co	69,000				69,000 S
X Y Co		65,000			
Minority 20% of $65,000 present surplus					13,000M
Elim. H. C. 80% of 60,000 surplus at acquisition				48,000	
H.C.Surplus 80% of $5,000 increase					4,000 S
P Q Co			20,000		
Minority 10% of $20,000 present surplus					2,000M
Elim. H. C. 10,750 surplus at acquisition				10,750	
H. C. Surplus					7,250 S
Current Accounts		25,000	35,000	60,000	
	$494,000	$220,000	$165,000	$288,750	$590,250

The various eliminations are based on surplus accounts at dates of acquisition, as follows:

X Y stock purchase on January 1, 1913:	Surplus of X Y Co. at that date	$60,000
P Q stock purchase on January 1, 1913:	Surplus of P Q Co. at that date	10,000
P Q stock purchase on June 30, 1913:	Surplus of P Q Company at that date:	
	Surplus at January 1	10,000
	Add one-half of 1913 profits	17,500
	Surplus at June 30	$27,500

To simplify the working papers, the various elements affecting the surplus at December 31, 1913, are combined as follows:

	A B Co.	*X Y Co.*	*P Q Co.*
Surplus, January 1, 1913	$50,000	$60,000	$10,000
Profits, 1913	44,000	45,000	35,000
Profit on sale of X Y Co. stock	5,000		
Total	99,000	105,000	45,000
Less Dividends paid in 1913	30,000	40,000	25,000
Surplus, December 31, 1913	$69,000	$65,000	$20,000

THE A B COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

December 31, 1913

Assets

Goodwill		$73,250
Properties		160,000
Current Assets		357,000
		$590,250

Liabilities

Capital Stock		$300,000
Surplus		80,250
Minority Interests:		
X Y Co.—20%	$33,000	
P Q Co.—10%	12,000	45,000
Accounts Payable		165,000
		$590,250

All stock purchases were made at less than book value. The excess of book value over cost is deducted from the holding company's goodwill account as a more conservative treatment than adding the excess to surplus.

Solution to problem 8.—The investment accounts appear to be carried at cost, and hence the book value of the stocks at the date of acquisition should be eliminated. The problem, however, does not contain any information as to the dates of acquisition nor the book value of the subsidiaries at the respective dates. Therefore all that can be done is to eliminate the entire cost of the stock from the investment accounts, and an equal amount from the subsidiaries' capital stock and surplus. If the holding company paid more than book value at the date of acquisition the elimination will be greater than it should be, with the result that the consolidated balance sheet will understate the goodwill and the surplus; on the other hand, if the holding company paid less than book value, the consolidated balance sheet will overstate the goodwill and the surplus.

The finished goods on consignment are carried at $100,000 while their cost was $60,000. The $40,000 unrealized profit will have to be eliminated, and no consideration should be given to the $10,000 estimated profit on realization.

Since the note brokers and bankers will lend money to individual companies and not to the organization as a whole, their security will depend upon the financial condition of the company to which the loan is made. Therefore it would be well to present these facts as well as the consolidated figures in the balance sheet, in columnar form, as shown on pages 210–211.

A B C MANUFACTURING COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

January 31, 1915

Assets	*A B C*	*Paris*	*Brown-Smith*	*Adjustments*	*I.-Co. Elim.*	*C. B. S.*	
Real Estate, Buildings, Machinery, etc.	$1,000,000	$250,000	$50,000			$1,300,000	
Goodwill	1,000,000	200,000				1,200,000	
Investment in Paris Mfg. Co. Stock—Cost	250,000						
Eliminate cost:							
Capital Stock*					$150,000		
Surplus					100,000		
Advances to Paris Mfg. Co	150,000				150,000		
Accounts Receivable	160,000	60,000	25,000			245,000	
Raw Material, Work in Process and Finished Materials	300,000	175,000	125,000			600,000	
Cash	50,000	25,000	25,000			100,000	
Investment in Brown-Smith Co. Stock—Cost	100,000						
Eliminate cost:							
Capital Stock					100,000		
Advances to Brown-Smith Co	100,000				100,000		
Finished Goods on Consignment			100,000	$40,000Cr.		60,000	
Deficit			50,000	40,000Dr.		90,000	S
	$3,110,000	$710,000	$375,000	0	$600,000	$3,595,000	

* In the absence of information, it is assumed that the holding company owns all of the stock of the Paris Manufacturing Company.

Liabilities	*A B C*	*Paris*	*Brown-Smith*	*Adjustments*	*I.-Co. Elim.*	*C. B. S.*	
Common Stock:							
A B C Manufacturing Company	$1,000,000					$1,000,000	
Paris Manufacturing Company		$150,000					
Eliminate holding company's 100%					$150,000		
Brown-Smith Company			$100,000				
Eliminate holding company's 100%					100,000		
Preferred Stock—7% Cumulative	1,000,000					1,000,000	
First Mortgage 6% Gold Bonds	500,000					500,000	
Notes Payable	250,000	90,000	150,000			490,000	
Accounts Payable	50,000	10,000	25,000			85,000	
Reserve for Bad Debts	10,000	10,000				20,000	
Surplus:							
A B C Manufacturing Company	300,000					300,000	S
Paris Manufacturing Company		300,000					
Eliminate surplus in cost of H. C. holdings					100,000		
Holding company surplus						200,000	S
A B C Manufacturing Company		150,000	100,000		250,000		
	$3,110,000	$710,000	$375,000	0	$600,000	$3,595,000	

THE A B C MANUFACTURING COMPANY AND ITS SUBSIDIARIES

(The Paris Manufacturing Company and The Brown-Smith Company)

CONSOLIDATED BALANCE SHEET

January 31, 1915

Assets	*A B C*	*Paris*	*Brown-Smith*	*Consolidated Balance Sheet*	
Fixed Assets:					
Goodwill	$1,000,000	$200,000		$1,200,000	
Real Estate, Buildings, Machinery, etc.	1,000,000	250,000	$50,000	1,300,000	
Total Fixed Assets	$2,000,000	$450,000	$50,000		$2,500,000
Current Assets:					
Accounts Receivable	$160,000	$60,000	$25,000	$245,000	
Less Reserve for Bad Debts	10,000	10,000		20,000	
	150,000	50,000	25,000	225,000	
Raw Material, Work in Process and Finished Goods	300,000	175,000	125,000	600,000	
Finished Goods on Consignment			60,000	60,000	
Cash	50,000	25,000	25,000	100,000	
Total Current Assets	$500,000	$250,000	$235,000		985,000
Inter-Company Current Accounts:					
Advances to Paris Manufacturing Company	$150,000				
Advances to Brown-Smith Company	100,000				
	$250,000				
Total All Assets	$2,750,000	$700,000	$285,000		$3,485,000

Liabilities	*A B C*	*Paris*	*Brown-Smith*	*Consolidated Balance Sheet*	
Fixed Liabilities:					
First Mortgage 6% Gold Bonds	$500,000				$500,000
Current Liabilities:					
Notes Payable	$250,000	$90,000	$150,000	$490,000	
Accounts Payable	50,000	10,000	25,000	85,000	
Total Current Liabilities	$300,000	$100,000	$175,000		575,000
Inter-Company Current Accounts:					
Due to the A B C Manufacturing Company		$150,000	$100,000		
Total All Liabilities	$800,000	$250,000	$275,000		1,075,000
Capital Stock in hands of the public:					
7% Cumulative Preferred	$1,000,000			1,000,000	
Common	1,000,000			1,000,000	2,000,000
Surplus: (Subject to preferred dividends since March 31, 1914)					410,000
					$3,485,000

CERTIFICATE

I have audited the books of the A B C Manufacturing Company for the (year presumably) ending January 31, 1915, as well as the books of its subsidiaries for the same period. These subsidiaries are the Paris Manufacturing Company and the Brown-Smith Company, the entire stock issues of both companies being owned by the A B C Manufacturing Company. I hereby certify that the foregoing Consolidated Balance Sheet is in my opinion a correct statement of the financial condition of the several companies and of the consolidation as a whole.

Solution to problem 9.—

THE SAFETY RAZOR COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET—WORKING PAPERS

December 31, 1912

Assets	*S. R. Co.*	*L W Co.*	*S. B. Co.*	*Adjustments* Dr.	Cr.	*I.-Co. Elim.*	*C. B. S.*
Investments in Stock of L W and Steel Blade (100%)							
4,000 shares of L W Co. and 4,000 shares of Steel Blade Co.	$2,500,000						
2,000 shares of Steel Blade Co		$400,000					
Eliminate L W Co. book entry writing up S. B. stock					$100,000(A)		
Eliminate book value at acquisition by S. R. Co. (April 1).							
Capital stock—L W Co						$400,000	
Capital stock—Steel Blade Co						600,000	
Surplus: L W Co.:							
Surplus, January 1, 1912 $605,000							
Less write-up of S. B. stock 100,000							
Net $505,000							
Add Profits to March 31, 1912 30,000						535,000	
Deficit: Steel Blade Co.:							
Deficit, January 1, 1912 $50,000							
Loss to March 31, 1912 15,000						65,000*	
Goodwill							$1,330,000 G
							25,000 S
Administration Expense	25,000						
L W Co. Current Account	100,000		195,000			295,000	
Steel Blade Company—Advances	150,000					150,000	
Cash	270,000	90,000	10,000				370,000
Organization Expense	75,000						75,000
Properties and Plant		325,000	325,000				650,000
Goodwill		250,000	50,000				300,000 G
Inventories		250,000	190,000	$10,000(B)			450,000
Receivables		195,000	105,000				300,000
	$3,120,000	$1,510,000	$875,000	$10,000	$100,000	$1,915,000	$3,500,000

THE SAFETY RAZOR COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET—WORKING PAPERS—*Continued*

December, 31 1912

Liabilities	*S. R. Co.*	*L W Co.*	*S. B. Co.*	*Adjustments Dr.*	*Adjustments Cr.*	*I.-Co Elim.*	*C. B. S.*
Adjustment columns forwarded				$10,000	$100,000		
Preferred Stock	$1,500,000						$1,500,000
Common Stock:							
Safety Razor Co.	1,500,000						1,500,000
L W Company		$400,000					
Eliminate 4,000 shares owned by S. R. Co.						$400,000	
Steel Blade Co.			$600,000				
Eliminate 4,000 shares owned by S. R. Co.						400,000	
Eliminate 2,000 shares owned by L W Co.						200,000	
Accounts Payable	20,000	125,000	90,000				235,000
Dividends from Subsidiaries	100,000						100,000 S
Steel Blade Co.		175,000			20,000(B)	195,000	
Safety Razor Co.		100,000	150,000			250,000	
Surplus:							
L W Co.		710,000			10,000(B)		
Less write-up of Steel Blade Co. stock					100,000(A)		
Eliminate surplus at date of acquisition—April 1						535,000	65,000 S
H. C. Surplus ($590,000—$535,000)			35,000				
Steel Blade Co.						65,000*	
Eliminate deficit at date of acquisition—April 1							100,000 S
H. C. Surplus—gain since April 1							
	$3,120,000	$1,510,000	$875,000	$120,000	$120,000	$1,915,000	$3,500,000

Explanation of Adjustments:

(A) Debit L W Surplus, credit Investment in Steel Blade Co. Stock, to reverse entry writing up stock and re-state the investment account at cost.

(B) Debit Inventories for merchandise in transit $10,000, debit L W Surplus for rent of warehouse $10,000, and credit Steel Blade Co. current account to reconcile with reciprocal current account.

THE SAFETY RAZOR COMPANY
AND ITS SUBSIDIARIES, THE L W COMPANY AND THE STEEL BLADE COMPANY

CONSOLIDATED BALANCE SHEET

December 31, 1912

Assets

Fixed Assets:		
Goodwill	$1,630,000	
Properties and Plant	650,000	$2,280,000
Current Assets:		
Inventories	450,000	
Receivables	300,000	
Cash	370,000	1,120,000
Deferred Charges:		
Organization Expense		75,000
		$3,475,000

Liabilities

Capital:		
Preferred Stock	1,500,000	
Common Stock	1,500,000	
Surplus	240,000	3,240,000
Current Liabilities:		
Accounts Payable		235,000
		$3,475,000

Some portion of the organization expense should perhaps be written off, but as this is a matter which lies within the discretion of the directors of the Safety Razor Company, and as they have apparently taken no action in regard to it, the entire $75,000 is carried as a deferred charge.

In solving this problem it is necessary to make an assumption as to the date when the L W Company made its entry adding $100,000 to the carrying value of its investment in the Steel Blade Company stock and to its surplus. This is imperative in order to determine the true book value of the L W Company at the first of April when the Safety Razor Company acquired the L W Company stock. The problem states that the L W Company had a surplus of $605,000 at January 1, 1912. If the $100,000 entry was made prior to that date, the true surplus at January 1 was $505,000, to which would be added the $30,000

profits of the first three months to determine the surplus at April 1. The working papers are prepared on the assumption that the write-up was made prior to January 1, 1912. On the other hand, if the entry was made in 1912, the true surplus of the L W Company at January 1 was $605,000 and the surplus at April 1 was $635,000, making the goodwill under this assumption $1,530,000, instead of $1,630,000.

This problem is complicated by the fact that the L W Company is a subsidiary so far as its relations with the Safety Razor Company are concerned, and a holding company so far as its relations with the Steel Blade Company are concerned. Consequently there is an investment account to eliminate from the Safety Razor Company's balance sheet and also an investment account to eliminate from the L W Company's balance sheet. After writing off the $100,000 arbitrary addition to the L W Company's investment in Steel Blade stock, both of these investment accounts are carried at cost. Hence eliminations are made by deducting the book value, at the date of acquisition, of all stock held within the organization. Since the consolidated balance sheet is prepared from the viewpoint of the Safety Razor Company as the parent corporation, the date of its stock purchase governs and not the date when the L W Company acquired the Steel Blade stock. In other words, on April 1 the Safety Razor Company obtained control of all of the stock of both the L W Company and the Steel Blade Company; the total inter-company stock-holdings are represented by two accounts of $2,500,000 and $300,000 (after writing off $100,000). Hence the goodwill is computed as follows:

Investment Accounts (at cost):		
On Safety Razor Company's books	$2,500,000	
On L W Company's books	300,000	$2,800,000
Eliminate book value at date of acquisition by Safety Razor Co.:		
Capital Stock:		
L W Company	400,000	
Steel Blade Company	600,000	
Surplus:		
L W Company	535,000	
Steel Blade Company	65,000*	1,470,000
Goodwill		$1,330,000

Solution to problem 10.

THE JONES INVESTMENT COMPANY AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET—WORKING PAPERS—JUNE 30, 1916

Assets	*Jones*	*A Co.*	*B Co.*	*C Co.*	*Adjustments Dr.*	*Adjustments Cr.*	*I.-Co. Elim.*	*C. B. S.*
Investment in A Co. (60%)	$1,000,000					$100,000(A)		
Reduce to Cost by charge to Surplus								
Eliminate book value at acquisition:								
Capital stock							$600,000	
Surplus—60% of $200,000							120,000	
Goodwill								$180,000 G
Investment in B Co. (75%)	600,000							
Eliminate book value at acquisition:								
Capital stock							600,000	
Surplus—75% of $4,000							3,000	
Deduction from goodwill								3,000*G
Investment in C Co. (80%)	400,000							
Eliminate book value at acquisition:								
Capital stock							320,000	
Surplus—80% of $100,000							80,000	
Advances to A Co.	100,000						100,000	
Advances to C Co.	50,000						50,000	
Cash	50,000	$100,000	$10,000	$50,000				210,000
Accounts Receivable		100,000	50,000	100,000				250,000
Inventories		200,000	100,000	50,000				350,000
Plant		1,000,000	600,000	400,000		45,000(B)		1,955,000
Deficit			40,000		$45,000(B)			
Minority 25% of $85,000 Pres. Def.								21,250M
Elim. H. C. 75% of 4,000 Sur. at Acq.							3,000*	
H. C. Surplus 75% of $89,000 Decrease								66,750S
	$2,200,000	$1,400,000	$800,000	$600,000	$45,000	$145,000	$1,870,000	$3,030,000

THE JONES INVESTMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET—WORKING PAPERS—JUNE 30, 1916—*Continued*

Liabilities	*Jones*	*A Co.*	*B Co.*	*C Co.*	*Adjustments Dr.*	*Adjustments Cr.*	*I.-Co. Elim.*	*C. B. S.*
Adjustment totals forwarded					$45,000	$145,000		
Capital Stock:								
Jones Investment Co.	$2,000,000							$2,000,000
A Company		$1,000,000						
Eliminate holding company's 60%							$600,000	400,000M
Minority interest 40%								
B Company			$800,000					
Eliminate holding company's 75%							600,000	200,000M
Minority interest 25%								
C Company				$400,000				
Eliminate holding company's 80%							320,000	80,000M
Minority interest 20%								
Jones Investment Co.		100,000		50,000			150,000	
Surplus:								
Jones Investment Co.	200,000					100,000A		
Reserves for Inter-Co. Profit								
In Inventories: 75% of $10,000								7,500 R
On Construction: 60% of 15,000								9,000 R
Balance—Surplus								83,500 S
A Company		300,000						
Minority 40% of $300,000 Pres. Surp.								120,000M
Elim. H. C. 60% of 200,000 Surp. at Acq.							120,000	
Surplus 60% of $100,000 Increase								60,000 S
C Company				150,000				
Minority 20% of $150,000 Pres. Surp.								30,000M
Elim. H. C. 80% of 100,000 Surp. at Acq.							80,000	
Surplus 80% of $50,000 Increase								40,000 S
	$2,200,000	$1,400,000	$800,000	$600,000	$145,000	$145,000	$1,870,000	$3,030,000

COMMENTS

Adjustment (A) is a debit to the Jones Investment Company's Surplus and a credit to its account of investment in Stock of Company A, taking out of surplus the $100,000 write-up of the investment, and reducing the investment account to its cost to permit the determination of goodwill by eliminating book value at acquisition.

Adjustment (B) is a debit to Deficit and a credit to Plant of Company B, to record the fire loss.

The reserve for inter-company profit in inventories is necessitated by the fact that the B Company sold goods to the A Company during 1916, on which they made a profit of $10,000, and these goods remain in the A Company's inventory. 75 per cent of the $10,000 is an unrealized inter-company profit.

The reserve for inter-company profit on construction is necessitated by the fact that Company A made a profit of $15,000 by constructing a part of the plant of Company C. As the holding company owns 60 per cent of the stock of Company A, 60 per cent of the $15,000 is an unrealized inter-company profit.

THE JONES INVESTMENT COMPANY
AND SUBSIDIARY COMPANIES—CO. A, CO. B AND CO. C

CONSOLIDATED BALANCE SHEET

June 30, 1916

Assets

Fixed Assets:			
Goodwill		$177,000	
Plant	$1,955,000		
Less Reserve for Inter-Co. Profit	9,000	1,946,000	$2,123,000
Current Assets:			
Inventories	350,000		
Less Reserve for Inter-Co. Profit	7,500	342,500	
Accounts Receivable		250,000	
Cash		210,000	802,500
			$2,925,500

Liabilities

Capital:			
Capital Stock		$2,000,000	
Surplus		116,750	$2,116,750
Minority Interests:			
Company A—40%		520,000	
Company B—25%		178,750	
Company C—20%		110,000	808,750
			$2,925,500

JONES INVESTMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED SURPLUS STATEMENT—WORKING PAPERS

July 1, 1915—June 30, 1916

	Jones	*A Co.*	*B Co.*	*C Co.*	*Minority*	*I.-Co. Elim.*	*Consolidated*
Balances—July 1, 1915:							
Jones Inv. Co. (after reversing $100,000 stock write-up)	$100,000						$100,000
A Company		$200,000			$80,000	$120,000	
B Company			$4,000		1,000	3,000	
C Company				$100,000	20,000	80,000	
Add Profits—Six Months to December 31, 1915:							
A Company		180,000			72,000		108,000
B Company			46,000		11,500		34,500
C Company				25,000	5,000		20,000
Add Profits—Six Months to June 30, 1916							
Jones Investment Company	217,500					217,500	
A Company		220,000			88,000		132,000
C Company				25,000	5,000		20,000
Total Credits	$317,500	$600,000	$50,000	$150,000	$282,500	$420,500	$414,500
Deduct:							
Loss: Six Months to June 30, 1916			$85,000		$21,250		$63,750
Dividends:							
Jones Investment Co	$217,500						$217,500
A Company		$300,000			120,000	$180,000	
B Company			50,000		12,500	37,500	
Total Debits	$217,500	$300,000	$135,000		$153,750	$217,500	$281,250
Balances—June 30, 1916	$100,000	$300,000	$85,000*	$150,000	$128,750	$203,000	$133,250

Deduct Reserves for Inter-Company Profit:

In Inventories —75% of $10,000 profit made by Co. B on goods in Co. A's inventory	$7,500	
On Construction—60% of 15,000 profit made by Co. A on plant built for Co. C	9,000	$16,500
Surplus—per consolidated balance sheet		$116,750

THE JONES INVESTMENT COMPANY AND SUBSIDIARIES

CONSOLIDATED SURPLUS STATEMENT

July 1, 1915—June 30, 1916

Surplus, July 1, 1915			$100,000
Add Profits for the Year:			
For Six Months Ending December 31, 1915		$162,500	
For Six Months Ending June 30, 1916		88,250	
Total		250,750	
Less Unrealized Inter-Company Profit:			
In Inventories	$7,500		
On Construction	9,000	16,500	234,250
Total			334,250
Deduct Dividends Paid			217,500
Surplus, June 30, 1916			$116,750

Solution to problem 11.—Since there are no minority interests in the subsidiaries, it is not necessary to determine the profits of the individual companies; therefore this feature of the working papers is omitted. As the beginning of the period is also the date of acquisition, the so-called inter-company profit in the inventories at that date is not true inter-company profit, and no adjustment is made for it.

COMPANY A AND SUBSIDIARIES B AND C

CONSOLIDATED WORKING PAPERS

For the Year Ending December 31, 1920

Debits	*Co. A*	*Co. B*	*Co. C*	*Adjustments Dr.*	*Cr.*	*Eliminations*	*Cost of Sales*	*P. & L.*	*Balance Sheet*
Cash	$75,000	$50,000	$60,000						$185,000
Accounts Receivable	350,000	190,000	420,000			$55,000A			905,000
Notes Receivable	200,000	60,000	40,000						300,000
Inventory, Raw Material, Jan. 1, 1920	150,000	105,000	160,000				$415,000		
Purchases, Raw Material	650,000	400,000	510,000			575,000B	985,000		
Labor	450,000	320,000	370,000				1,140,000		
Manufacturing Expense	190,000	190,000	205,000				585,000		
Selling Expense	85,000	40,000	75,000					$200,000	
Administrative Expenses	45,000	25,000	35,000					105,000	
Inventory, Goods in Process, Jan. 1, 1920	80,000	70,000	75,000				225,000		
Inventory, Finished Goods, Jan. 1, 1920	90,000	65,000	80,000				235,000		
Plant and Equipment	900,000	400,000	750,000						2,050,000
Investment in Stock of Co. B (100%) Cost	875,000								
Eliminate book value at acquisition:									
Capital stock						500,000C			
Surplus at January 1, 1920						185,000D			
Goodwill									190,000 G
Investment in Stock of Co. C (100%) Cost	1,200,000								
Eliminate book value at acquisition:									
Capital stock						800,000E			
Surplus at January 1, 1920						347,500F			
Goodwill									52,500 G
	$5,340,000	$1,915,000	$2,780,000						

Inventories—December 31, 1920:									
Raw Materials	$280,000	$175,000	$210,000	$665,000(a)					$665,000
Goods in Process	95,000	80,000	85,000	260,000(a)					260,000
Finished Goods	135,000	145,000	105,000	385,000(a)					385,000
Bond Interest Accrued				12,500(b)				$12,500	
Depreciation on Plant and Equipment				102,500(c)			$102,500		
				$1,425,000	0	$2,462,500			
Total debits to Cost of Sales							3,687,500		
Less credits—per contra							1,240,000		
Cost of goods sold—to Profit and Loss							$2,447,500	2,447,500	
Total debits to Profit and Loss—deducted contra								$2,765,000	$4,992,500

COMPANY A AND SUBSIDIARY COMPANIES B AND C

CONSOLIDATED WORKING PAPERS—*Continued*

Credits	*Co. A*	*Co. B*	*Co. C*	*Adjustments Dr.*	*Adjustments Cr.*	*Eliminations*	*Cost of Sales*	*P. & L.*	*Balance Sheet*
Adjustment column totals forward				$1,425,000					
Capital Stock:									
Company A	$3,000,000								$3,000,000
Company B		$500,000							
Eliminate Co. A's 100%						$500,000C			
Company C			$800,000						
Eliminate Co. A's 100%						800,000E			
Notes Payable	110,000	80,000	60,000						250,000
Accounts Payable	100,000	65,000	250,000			55,000A			360,000
Bonds Payable	500,000								500,000
Premium on Bonds	5,000							$500	4,500
Reserve for Depreciation	100,000	60,000	112,500		$102,500(c)				375,000
Sales	1,400,000	1,050,000	1,250,000			575,000B		3,125,000	
Surplus:									
Company A	125,000								125,000 S
Company B		160,000							
Eliminate surplus at Jan. 1, 1920						185,000D			
Deduction from H. C. Surplus									25,000*S
Company C			307,500						
Eliminate surplus at Jan. 1, 1920						347,500F			
Deduction from H. C. Surplus									40,000*S
	$5,340,000	$1,915,000	$2,780,000						

Cost of Sales Credit for Inventories—Dec. 31, 1920:						
Raw Material	50,000(d)	665,000(a)		$615,000		
Goods in Process	11,000(d)	260,000(a)		249,000		
Finished Goods	9,000(d)	385,000(a)		376,000		
Reserve for Inter-Company Profit in Dec. 31, 1920 Inventories		70,000(d)				70,000R
Bond Interest Accrued		12,500(b)				12,500
	$1,495,000	$1,495,000	$2,462,500			
Total Credits to Cost of Sales—deducted contra				$1,240,000		
Total Credits to Profit and Loss					3,125,500	
Less Debits to Profit and Loss—per contra.					2,765,000	
Net Profit to Surplus						360,500
						$4,992,500

COMPANY A AND SUBSIDIARIES B AND C *Exhibit A*

CONSOLIDATED STATEMENT OF COST OF GOODS MANUFACTURED AND SOLD

For the Year Ending December 31, 1920

Goods in Process, January 1, 1920			$225,000
Materials:			
Inventory, January 1, 1920	$415,000		
Add Purchases	985,000		
Total	$1,400,000		
Less Inventory, Dec. 31, 1920	615,000	$785,000	
Labor		1,140,000	
Manufacturing Expense:			
Miscellaneous	585,000		
Depreciation of Plant and Equipment	102,500	687,500	2,612,500
Total Manufacturing Cost			2,837,500
Deduct Inventory, Goods in Process, December 31, 1920			249,000
Cost of Goods Manufactured			2,588,500
Add Inventory of Finished Goods, January 1, 1920			235,000
Total			2,823,500
Less Inventory of Finished Goods, December 31, 1920			376,000
Cost of Goods Sold			$2,447,500

COMPANY A AND SUBSIDIARIES B AND C *Exhibit B*

CONSOLIDATED PROFIT AND LOSS STATEMENT

For the Year Ending December 31, 1920

Sales			$3,125,000
Less Cost of Goods Sold (Exhibit A)			2,447,500
Gross Profit on Sales			677,500
Less Selling Expenses			200,000
Net Profit on Sales			477,500
Less Administrative Expenses			105,000
Net Profit on Operations			372,500
Less Bond Interest:			
Interest Accrued	$12,500		
Less Premium Amortized	500		12,000
Net Profit for the Year			$360,500

COMPANY A AND SUBSIDIARIES B AND C *Exhibit C*

CONSOLIDATED SURPLUS STATEMENT

Year Ending December 31, 1920

Surplus, January 1, 1920	$210,000
Add Profits for 1920 (Exhibit B)	360,500
Total	570,500
Less Dividends Paid	150,000
Surplus, December 31, 1920	$420,500

COMPANY A AND SUBSIDIARIES B AND C *Exhibit D*

CONSOLIDATED BALANCE SHEET

December 31, 1920

Assets

Current Assets:			
Cash		$185,000	
Accounts Receivable		905,000	
Notes Receivable		300,000	
Inventories:			
Raw Material	$665,000		
Goods in Process	260,000		
Finished Goods	385,000		
Total	1,310,000		
Less Inter-Company Profit	70,000	1,240,000	$2,630,000
Fixed Assets:			
Plant and Equipment		2,050,000	
Less Reserve for Depreciation		375,000	
		1,675,000	
Goodwill		242,500	1,917,500
			$4,547,500

Liabilities

Current Liabilities:		
Notes Payable	250,000	
Accounts Payable	360,000	
Accrued Bond Interest	12,500	622,500
Fixed Liabilities:		
Bonds Payable		500,000
Deferred Credits:		
Premium on Bonds		4,500
Capital:		
Capital Stock	3,000,000	
Surplus (Exhibit C)	420,500	3,420,500
		$4,547,500

COLUMBIA UNIVERSITY LIBRARY

This book is due on the date indicated below, or at the expiration of a definite period after the date of borrowing, as provided by the rules of the Library or by special arrangement with the Librarian in charge.

DATE BORROWED	DATE DUE	DATE BORROWED	DATE DUE
OCT 28 1942	~~Dec 4~~ Nov. 11		
JUL 7 1943	7/14		
JAN 31 1944	Feb. 14		
MAR 17 1944	Mar. 24		
MAY 25 1944	June 1		
JAN 13 1945	1/20		
JAN 22 1946			
APR 13 1948	4/22		
JUL 25 1948	8/1		
JAN 29 1947	2/17		
Nov 16 '53			

C28(239)M100

COLUMBIA UNIVERSITY
0032054289

MSH 00722.

NEH

MAR 16 1994

END OF
TITLE